January 1963
FEDERAL RESERVE BANK OF ST. LOUIS
Review

1962—A Year the Economy Marked Time

TWO IMPORTANT PROBLEMS faced the economy at the beginning of 1962: a relatively large proportion of unemployed resources and a continuing deficit in the balance of payments. Domestic business activity expanded early in the year, and there was an improvement in the nation's balance of payments. However, business activity moved along a plateau during the last seven months of the year, and after the second quarter the payments deficit rose. By the end of the year both the level of unemployment and the balance-of-payments deficit were little changed from a year earlier. Monetary and debt-management developments in 1962 are examined in the context of the domestic and international economic situations.

Chart on District and U. S. Labor Force and Employment appears on page 12

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P. O. Box 442 • St. Louis 66, Mo.

1962—A Year the Economy Marked Time

Introduction

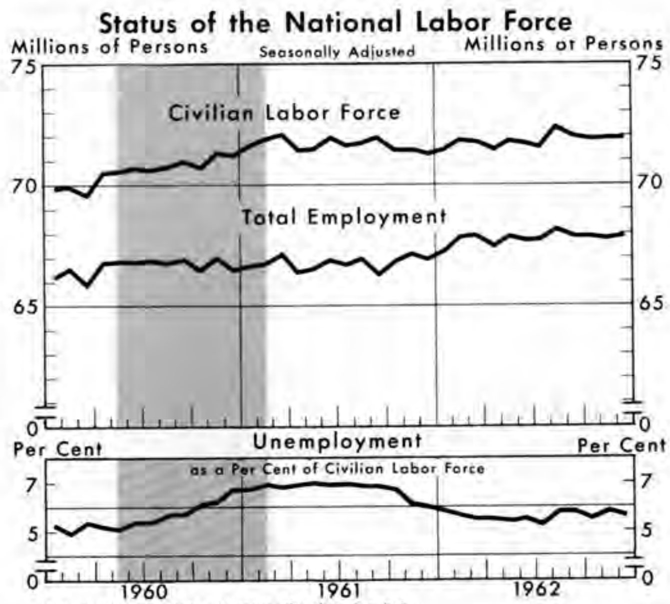
THE FIRST THREE YEARS of this decade have not seen the economic progress which had been anticipated. As the economy approached the 1960's optimism ran high that the next ten years would be a period of great growth and prosperity. The coming decade was commonly referred to as the "Soaring Sixties." However, economic activity turned down in June 1960, capping the shortest business expansion in the postwar period. The nation's balance of payments continued in a substantial deficit position, and strong concern developed over the state of the dollar as the world's primary reserve currency.

The business recession which began in mid-1960 proved mild in length and severity. In early 1961 activity turned up and rose steeply throughout the year. By the end of 1961 prerecession levels had been surpassed and the earlier optimism as to the economy's prospects again appeared to be justfied. The year 1962 was widely expected to be one of rapid economic expansion, prosperity, and improvement in the balance of payments.

During the first five months of 1962 economic activity rose, but the expansion had lost some of its earlier vigor. From December 1961 to May 1962 industrial production rose at an annual rate of 6 per cent, compared with a 14 per cent rate in the previous ten months. From about May to the end of 1962 the economy marked time. Industrial production inched up about 1 per cent from May to July and then remained virtually unchanged through December.

Source: Board of Governors of the Federal Reserve System
Latest data plotted: December estimated
Shaded area represents period of business recession.

Although the plateau in activity from late spring to the end of the year followed more than a year of expansion, it was not high enough to bring about an acceptable degree of resource utilization. The unemployment rate, which declined from 5.8 per cent during the early part of the year to 5.4 per cent in May and 5.3 per cent in July, rose in midsummer and fluctuated near the 5.8 per cent level from August to year end. One-fifth of the capacity in major materials-producing industries remained unused.



Source: United States Bureau of Labor Statistics
Latest data plotted: December estimated

The United States continued to suffer an adverse balance of payments throughout 1962. A favorable balance of trade was more than offset by U. S. investments abroad, costs of maintaining our military establishment overseas, foreign aid, and other factors. This payments deficit was financed both by net sales of gold to foreign official institutions and by increases in foreign dollar holdings. Taking the year 1962 as a whole, our net payments position was roughly the same as in 1961, but was substantially better than in 1958, 1959, and 1960.

The possibility of short-term capital outflows continued to be a major concern of the Government throughout 1962. These capital movements are influenced by the elements of confidence, exchange crises in other countries, and temporary opportunities for gain arising from interest differentials. Despite the break in the stock market, the Canadian exchange crisis, and the Cuban situation, no massive short-term capital outflows, such as had marked 1961, developed. Some outflows occurred, reflecting the relatively high short-term interest rates in the United Kingdom and Canada.

Policy Objectives

Average prices in this country were relatively stable during 1962, and maintenance of price stability was therefore of secondary importance in formulating economic policy. By contrast, avoidance of price inflation had been a foremost consideration in most other postwar years.

Government economic policy during 1962 was faced with two basic tasks. One was to stimulate domestic economic activity. The other was to reduce the balance-of-payments deficit. It is within the framework of these problems that monetary, debt management, and fiscal actions were conducted.

Actions which might have contributed to the solution of one problem were frequently at variance with the solution to the other problem. For example, with reference to domestic weakness, monetary theory called for expansive action by the Federal Reserve System. This involved increasing the supply of member bank reserves. With additional reserves, member banks would be encouraged to expand loans and investments and, hence, increase deposits.[1] Large-scale monetary expansion, in turn, implied lower interest rates as a short-run consequence. Lower short-term interest rates, however, were likely to increase the net outflow of funds from the country.

Other Government actions did not involve this conflict. Treasury debt-management operations increasing the short-term debt gave some upward pressure to short-term interest rates, making transfers of funds out of the country less attractive, while adding to the liquid asset holdings of the public, thereby stimulating domestic activity. With respect to the unfavorable balance of payments, the Government adopted a wide variety of measures which work gradually over a period of time. These included actions to limit Government spending abroad and to obtain offsetting receipts from prosperous allies, vigorous promotion of exports, and reduction of tax incentives for American investment in developed foreign countries. The Treasury liberalized its depreciation allowances and Congress enacted a tax credit for new investment; both of these actions may have helped to stimulate the domestic economy.

The tactical objective of the monetary authorities since about mid-1960 has been to achieve an expansion in bank reserves, bank credit, and the money supply without creating a downward movement in short-term interest rates. It was felt that this combination of proximate objectives would contribute to the solution of both basic problems. Such a mix of objectives may be attained by supplying reserves only during periods when there is an upward pressure on interest rates. This may require the central bank to await developments which, of themselves, produce an upward pressure on interest rates, such as a seasonal or cyclical rise in credit demands. Alternatively, Government itself may put an upward pressure on short-term interest rates. This it may do by increasing the volume of short-term Treasury obligations. Such an increase in short-term obligations may involve the creation of additional Treasury debt, either to finance a cash deficit or to build up cash balances, or may simply involve a shift in the maturity structure of the outstanding debt. During periods when there are upward pressures on interest rates, whether the forces producing these pressures are seasonal, cyclical, or the result of Government action, reserves and money may be expanded without a decline in rates.

The Reserve System can provide banks with reserves without putting direct and immediate downward pressure on short-term interest rates. One method is to reduce reserve requirements. This "unlocks" reserves, for bank credit and deposit expansion, without direct participation by the central bank in short-term markets. The Reserve System may also provide bank reserves by purchasing intermediate- and long-term securities. Initially, this technique also avoids direct pressure on short-term interest rates. However, with respect to either of these methods, to the extent that asset purchases by banks are conducted in markets for short-term debt instruments, downward pressure may be brought to bear on short-term rates.

[1] For a description of the mechanics of deposit creation, see *The Federal Reserve System: Purposes and Functions,* Board of Governors of the Federal Reserve System.

From the End of 1961 to Late Spring 1962

The following analysis describes economic events of 1962 in terms of two time periods. The first is the period of expansion in economic activity which took place during the first five months of the year. The second is the interval from around May to the end of 1962 in which only minor advances were registered in most areas of the economy. Within each of these time periods there is a discussion of business developments along with an analysis of significant factors which affected the balance of payments. Monetary and debt-management actions are examined within the general context of these economic developments.

Domestic Business Conditions

Business activity expanded through the first few months of 1962. This expansion was a continuation at a reduced pace of the cyclical upswing which began in February 1961. Total expenditures on goods and services increased $13.4 billion from the fourth quarter of 1961 to the second quarter of 1962, or at a 5 per cent annual rate. In the previous two quarters these expenditures rose at a 10 per cent rate. Employment, which had fluctuated near the 67 million mark from February to December 1961, rose to 68 million by February 1962 and remained near this level. Unemployment declined from 5.8 per cent of the civilian labor force in January 1962 to 5.4 per cent in May.

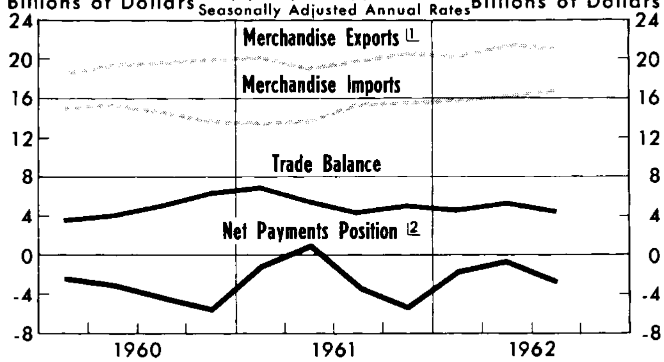
The rise in activity during the winter and early spring of 1962 was fostered by an inventory buildup in anticipation of a possible steel strike. Also, expenditures by the Treasury exceeded tax and other receipts, seasonally adjusted, adding to the demand for goods and services. The Federal cash deficit, incurred at a $6.0 billion annual rate during the last half of 1961, rose to a $12.8 billion annual rate during the first quarter of 1962. Another factor contributing to economic expansion may have been the rapid rise in the money stock during the fall of 1961; from August to December 1961 the money supply expanded at a 6 per cent annual rate. This increase in actual money balances may have been more rapid than the rise in desired balances, contributing to an expansion in spending.[2]

[2] See the June 1962 *Review* of this Bank on "Velocity of Money 1951-1962."

International Developments

The international payments situation of the United States was marked by a declining deficit during the first half of 1962. In the fourth quarter of 1961, the U. S. payments deficit amounted to an annual rate of $5.6 billion. In the first quarter of 1962 it dropped to $1.9 billion and in the second quarter to $0.9 billion. Although the balance-of-trade surplus in the first quarter of 1962 was slightly lower than in the fourth quarter of 1961, its decline was more than offset by improvement in net receipts on investment income, a decline in Government grants and capital outflows, and a rise in foreign investment in the United States.

United States Balance of Trade and Net Payments Position



1 Excluding military transfers under grants.
2 Deficit measured by net decline in U.S. gold and net increases in foreign-held dollar assets. Since 1961 gold sales are net of change in convertible currencies held by Exchange Stabilization Fund.
Source: U.S. Department of Commerce
Latest data plotted: 3rd Quarter preliminary

The reduction in the deficit for the second quarter reflected primarily: (1) a rising trade surplus moving from an annual rate of $4.3 billion in the first quarter to $5.3 billion in the second quarter, (2) a decline in the net outflow of U. S. short-term private capital reflecting a cessation of Japanese borrowing from U. S. commercial banks and the impact of the Canadian exchange crisis, and (3) foreign repayments on U. S. Government loans.

During the first half of 1962 there was an uneasy atmosphere in the foreign exchange markets. Early in the year short-term funds moved from the Continent to New York and London. Following the Canadian exchange crisis and the stock market breaks in May and June, short-term funds began to flow in volume to the Continent.

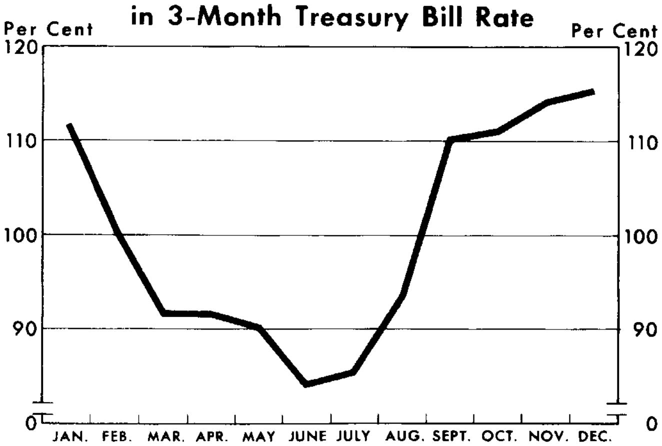
The United States authorities cooperated in the task of dampening potentially disruptive short-term foreign exchange disturbances by buying and selling foreign exchange. The underlying purpose of these official transactions was to assist in maintaining international exchange rate stability and to offset or compensate for, when appropriate, the effects on U. S. gold reserves of sudden fluctuations in the international flow of payments. The U. S. Treasury in 1961 initiated United States participation in foreign exchange transactions. In February 1962 the Federal Reserve's Open Market Committee authorized the Federal Reserve Bank of New York to undertake transactions in foreign currencies for System Open Market Account in accordance with the Committee's instructions.

Under this authorization the System moved to acquire foreign currency balances. Initially, small amounts of several convertible currencies were purchased from the United States Treasury. Then, additional resources became available through a series of currency swap arrangements concluded with leading central banks. Using its newly gained resources, the System on several occasions during the first half of 1962 operated in the New York foreign exchange market to moderate temporary disturbances.

Interest Rates

Monetary and debt-management actions were conducted in the light of the environment outlined above. The chief goals were to promote a continued rise in economic activity without causing an increase in the net outflow of funds. While taking expansive actions to stimulate domestic economic activity, it was deemed necessary to minimize downward pressure on short-term interest rates. Business activity, which was rising cyclically, put some moderate upward pressure on rates. On the other hand, as the accompanying chart demonstrates, seasonal forces during the early months

Seasonal Fluctuations in 3-Month Treasury Bill Rate



of the year exert strong downward pressure on short-term rates. It appears that in early 1962 the seasonal forces were somewhat stronger than the cyclical forces.

Yields on three-month Treasury bills fluctuated near the 2.70 per cent level during the first six months of 1962. From mid-1960 until late 1961 rates on these securities had been relatively stable, moving within the 2.20-2.40 per cent range. From October 1961 to the end of the year yields on three-month Treasury bills moved up to the 2.70 per cent level.

As Table I shows, interest rates on debt instruments outside the short end of the maturity spectrum did not display the same relative stability as the bill rate. Yields on long-term bonds drifted lower from December to May. This behavior of the rate structure was the result of many factors. In addition to seasonal and cyclical business forces, Treasury debt-management operations and actions of the banking system must be considered.

TABLE I

Selected Interest Rates
(Monthly averages of daily figures)

	Months	3-Month Treasury Bills	3-5 Year Government Issues	High-Grade Municipal Bonds
1961:	Dec.	2.60	3.82	3.49
1962:	Jan.	2.72	3.84	3.32
	Feb.	2.73	3.77	3.28
	Mar.	2.72	3.55	3.19
	Apr.	2.73	3.48	3.08
	May	2.68	3.53	3.09

The Treasury's handling of the debt placed upward pressure on short-term interest rates in the first five months of the year. From December to May the public's holdings of Government debt maturing within 1 year expanded by about $4 billion. During this same period there was a decline of about $3.5 billion in Federal debt maturing in more than one year, with much of the decline occurring within the 1- to 5-year maturity range.

Bank portfolio adjustments relating to the rapid growth in time deposits during the early months of 1962 were made without placing much downward pressure on short-term interest rates. Effective at the beginning of 1962 there was a change in Federal Reserve Regulation Q raising the maximum allowable interest on time deposits from 3 per cent to 4 per cent. One purpose of the change was to enable banks to compete more vigorously to retain foreign deposits.[3] Time deposits had been increasing at an

[3] Another purpose of this change in Regulation Q was to allow banks to compete more effectively for savings-type deposits.

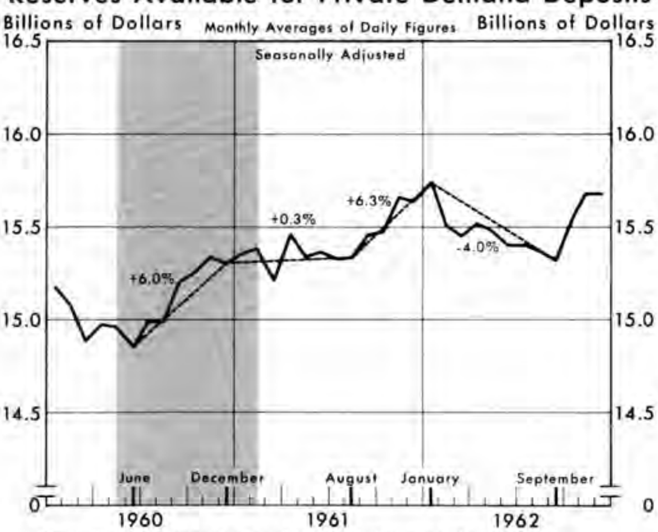
11 per cent annual rate since mid-1960; but in the first five months of 1962 they rose at a 20 per cent rate.

With the expansion in time deposits, banks increased their demand for mortgages and for longer term municipal and Government debt instruments. These purchases served to bid up prices (depress yields) on securities outside the short-term sector. The banking system, as it shifted its net purchases into longer term issues, removed a potential downward pressure on short-term rates.

Monetary Developments

Federal Reserve policies during the early months of 1962 provided reserves to the banking system in ways that minimized downward pressures on short-term interest rates. Actions taken pursuant to these policies resulted in some increase in total member bank reserves. This moderate increase in total reserves, coupled with the rapid growth in time deposits which require a smaller reserve backing than demand deposits, resulted in an expansion of total bank credit at a 9 per cent annual rate. However, the rise in reserves was less than the volume needed to support the increases in time and U. S. Government deposits. Consequently, reserves available for privately held demand deposits (the major part of the money supply) declined at an annual rate of 2.5 per cent from December 1961 to May 1962.

Reserves Available for Private Demand Deposits

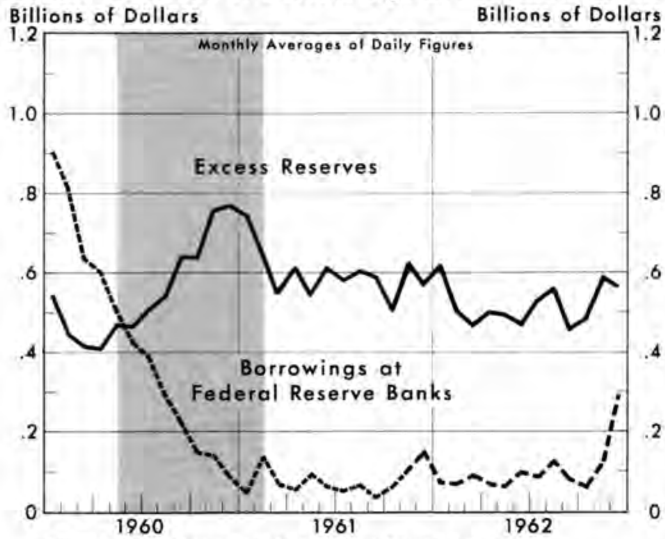


Percentages are annual rates of change between months indicated.
Latest data plotted: December estimated

During the first five months of the year gross System open market operations were conducted largely in short-term securities. However, on balance, the Federal Reserve increased its holdings of securities maturing within 1 to 5 years, while there was little net change in holdings of securities in other maturity ranges. Normally, open market operations are conducted almost exclusively in short-term securities, primarily Treasury bills. This venture into the intermediate sector permitted the System to expand reserves while limiting the initial impact of such action on short-term rates.

From January to May excess reserves of member banks averaged about $500 million, near the average of the past decade. During this period member bank borrowings from Reserve Banks remained nominal, since short-term interest rates were less than the discount rate. Free reserves, the difference between excess reserves and borrowings, averaged about $400 million in the January-to-May 1962 period. This relatively high level of free reserves was unusual for this stage of the business cycle, reflecting primarily the unusually small amount of borrowing from the Federal Reserve.

Excess Reserves & Borrowings of Member Banks



Source: Board of Governors of the Federal Reserve System
Latest data plotted: December estimated

Total bank loans and investments rose at a 9 per cent annual rate from December 1961 until May 1962. Bank loans, particularly to businesses and on real estate, rose substantially, and banks increased their holdings of municipal securities. This expansion reflected the moderate rise in total bank reserves and a sharp increase in time deposits which require lower average reserves.

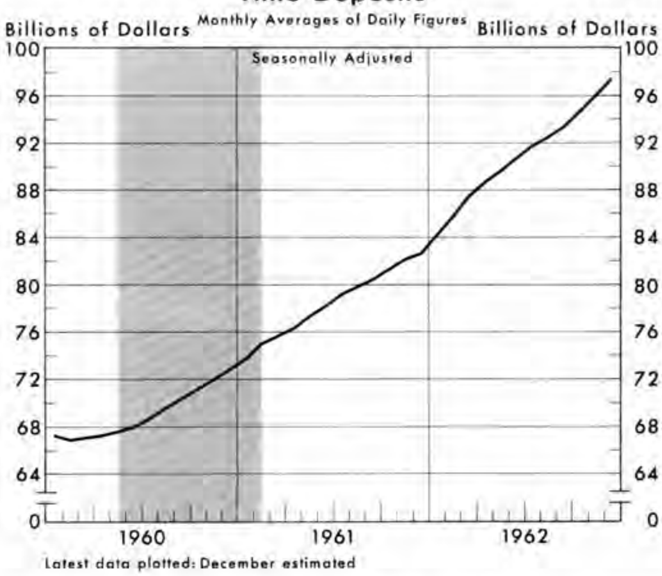
The Public's Liquidity

One way of viewing financial developments is to examine the public's holdings of "monetary assets." According to this view, a rise in the public's holdings of these assets relative to its demand for them results in a rise in spending, including an increase in the demand for goods and services.[4] The unique feature of monetary assets is that the central bank can affect the quantity which the public holds relative to the quantity it desires to hold. Adjustments to discrepancies between desired and actual holdings take the form of some combination of adjustments in financial investment and expenditures on goods and services.

The money supply (demand deposits and currency) of the nation was about unchanged during the first five months of 1962. The average rate of growth in money during the previous decade was 2.1 per cent. There have been other periods since 1951 when the money stock has failed to grow for periods of five months or longer. These periods were from June 1953 to April 1954, December 1956 to January 1958, and from July 1959 to June 1960. During and immediately following each of these periods there was a slackening in economic activity.[5]

Time and savings deposits expanded at an accelerated rate during the first five months of 1962, reflecting in part the change in Federal Reserve regulations which permitted higher interest rates to be paid on these deposits. Savings deposits and time certificates of deposit shared about equally in this expansion in contrast with the dominant role played by passbook

Time Deposits



savings accounts in the preceeding year.[6] The issuance of negotiable certificates of deposit by many money market banks and the development of a market for such certificates probably enhanced the desirability of these instruments. Time certificates of deposit, particularly negotiable certificates of large denomination, are held largely by investors who are sensitive to interest rate differentials.

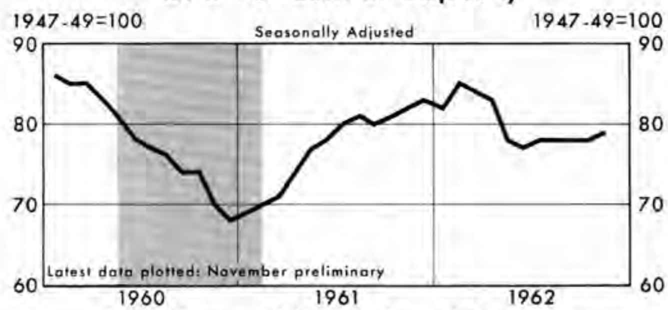
From Late Spring to the End of 1962

Business Activity

From May to the end of 1962 the tempo of business activity slackened further. Industrial output edged upward from May to July, and then remained on a plateau during the last half of the year. Employment, which had been near the 68 million level since February, remained virtually unchanged from May to the end of 1962. Personal incomes increased at less than a four per cent annual rate from May to December, in contrast to a 7 per cent rate of increase in the previous 15 months. Total production of goods and services, gross national product, rose at about a 3 per cent annual rate from the second to the fourth quarter of 1962, as against a 7.6 per cent rise in the previous year.

The amount of unemployed resources increased during the second half of 1962. The unemployment rate, which had declined during the first six months, reaching 5.4 per cent in May and 5.3 per cent in July, rose to 5.8 per cent in August. The rate then fluctuated near this level during the remainder of the year. Unused capacity in major materials industries also increased during the period.

Major Material Output as a Per Cent of Capacity



Source: Board of Governors of the Federal Reserve System

There were several factors which may have contributed to the hesitation in business activity during late 1962. With incomes rising in the early part of the year, tax receipts of the Federal Government increased sharply. As a result, the Federal cash deficit declined from a $12.8 billion annual rate in the first quarter to an estimated $1.0 billion annual rate during the rest of the year. The rise in steel inventories during the first quarter of the year came to an abrupt

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[4] See the June 1962 *Review* of this Bank on "Velocity of Money 1951-1962."

[5] See "Member Bank Reserves and the Money Supply 1951-62," in the March 1962 monthly *Review* of this Bank.

[6] See "Recent Growth of Time Deposits," in the April 1962 issue of this *Review*.

U.S. Government Cash Budget

Source: U. S. Treasury Department
Latest data plotted: 4th Quarter preliminary

end as wage negotiations were completed in the spring and a midsummer strike was avoided. Steel inventories were worked down through the second and much of the third quarter, and steel production was curtailed sharply from about March through July. The lack of growth of the public's money supply in the first five months of 1962 (mentioned above) continued through August. The supply of money may have declined relative to the demand for it, even though time deposits and other liquid assets, generally regarded as close substitutes for money, rose rapidly.

Stock prices began a decline in the early spring which culminated in a rapid fall during late May and

Stock Prices*

*Standard & Poor's 500 Stocks
Latest data plotted: December

early June. The Standard and Poor's index of 500 stocks moved from an average of 70.3 in March to 55.6 in June, reaching a low of 53.3 during the week ending June 29. Common stocks are an important form in which the public holds its wealth. Movements in stock prices, increasing or decreasing wealth, may have a significant influence both on consumer spending and on stock flotations and business capital expenditures.

International Developments

There was a deterioration in the net-payments position from the second to the third quarter of 1962. A primary factor in this deterioration of the overall balance was the swing in transactions reflecting the Canadian exchange crisis which ended late in June. The third-quarter flow of net payments to Canada more than offset the receipts from advance debt repayments by France and Italy.

In the spring the United States balance of trade improved as merchandise exports spurted upward to more than offset the continuing increase in imports. Exports to Canada jumped in part because shipments were speeded up to anticipate impending Canadian crisis measures. Exports to Europe also showed unusual strength in the spring as poor European harvests and anticipated Common Market import regulations stimulated heavy grain shipments from the United States.

The trade balance became less favorable in the third quarter as merchandise imports continued to rise in the face of falling exports. Export volume was adversely affected by the devaluation of the Canadian dollar and the new Canadian import restrictions. Export weakness in the third quarter also reflected the absence of those special factors which had stimulated the heavy volume of exports to Canada and Europe in the second quarter.

A large inflow of short-term capital from Canada occurred during the first half of 1962, resulting in part from that country's exchange crisis. As Canadian policies associated with the devaluation of the Canadian dollar proved successful there was a reflux of short-term funds to Canada during the third quarter. Short-term funds moved to Canada attracted in part by the higher interest rates established there as a part of the measures taken by the Canadian Government to defend the exchange value of its currency.

Interest Rates

In the period from May to the end of 1962 there was a rise in short-term rates and a decline in long-term rates. This change in the yield curve is shown in the accompanying chart. Yields on three-month Treasury bills rose from the 2.70 per cent level in the first five months of the year to a range of about 2.75 to 2.90 per cent in the last seven months of the year. Bill rates were relatively high in the range in late June and July and again in November and December when the Treasury was a large borrower of short-term funds. Interest rates on most longer term issues rose slightly

Source: Board of Governors of the Federal Reserve System

from May to July but then drifted lower during the rest of the year.

This shift in the yield curve reflected many forces. On the one hand, there was a seasonal increase in the demand for credit as crops moved to market, as Treasury expenditures exceeded receipts, and as businesses prepared for the Christmas bulge in spending. These seasonal credit demands placed an upward pressure on short-term interest rates. Treasury management of the public debt reduced the outstanding supply of issues maturing in less than 5 years but at the same time increased the supply of Treasury bills as well as issues of over 5 years maturity. This action placed upward pressures on very short-term and long-term interest rates and downward pressure on other rates.

Cyclical developments in business and monetary expansion also contributed to shifting the yield curve. With the pace of business expansion slowing, demands for funds may have weakened somewhat. However, with the upward seasonal pressures being exerted on short-term rates, the Federal Reserve System was able to expand bank reserves markedly in the fall of the year and thereby help to stimulate domestic activity. By themselves, these actions tend to place downward pressure on interest rates. However, the Federal Reserve took steps to attain the reserve expansion in such a way as to reduce these downward pressures. Some reserves were supplied by net purchases outside the short-term sector. Additional reserves were made available through reducing the required percentage of reserves that member banks must hold behind time deposits from 5 to 4 per cent.

Monetary Developments

With the two basic problems of unemployed resources and the deficit in the balance of payments persisting during the last seven months of 1962, there was little change in the overriding focus of Government actions. Policies designed to stimulate domestic economic activity were modified by balance-of-payments considerations, especially as actions taken affected domestic short-term interest rates vis-a-vis short-term rates in foreign money market centers.

Total member bank reserves were little changed from May to August of 1962. Reserves available to support privately held demand deposits continued to decline during this period, as Treasury balances and time deposits grew rapidly. From August to the end of the year, however, total reserves increased at a steep 6 per cent annual rate. After adjusting for reserves needed to support Treasury and time deposits (not included in the usual definition of the money supply), reserves available to support privately held demand deposits rose at an annual rate of 5.6 per cent.

In order to provide comparable figures, adjusted for the recent change in reserve requirements, reserves previous to November 1 were reduced by 1 per cent of time deposits (for the week of October 25-31, 1 per cent of country banks only).
Latest data plotted: December estimated

The growth of total reserves beginning in August occurred without any significant change in the net reserve positions of member banks. As in the early part of the year, excess reserves continued to fluctuate around $500 million, near the amount member banks customarily hold. Borrowings from the Federal Reserve Banks continued to average less than $100 million, as short-term money market rates remained below the discount rate.

Total bank loans and investments grew at a rapid pace from May to the end of 1962, continuing the expansion which had characterized the first five months of the year. Advances to businesses and on real

FEDERAL RESERVE SYSTEM ACTIONS DURING 1962

Discount Rate

In effect January 1, 1962	3%
In effect January 1, 1963	3%

Reserve Requirements

	Percentage Required			
	Demand Deposits		Time Deposits	
	Reserve City Banks	All Other Member Banks	Reserve City Banks	All Others Member Banks
In effect January 1, 1962	16½	12	5	5
October 25, 1962			4	
November 1, 1962				4
In effect January 1, 1963	16½	12	4	4

Margin Requirements on Stocks

In effect January 1, 1962	70%
July 10, 1962	50%
In effect January 1, 1963	50%

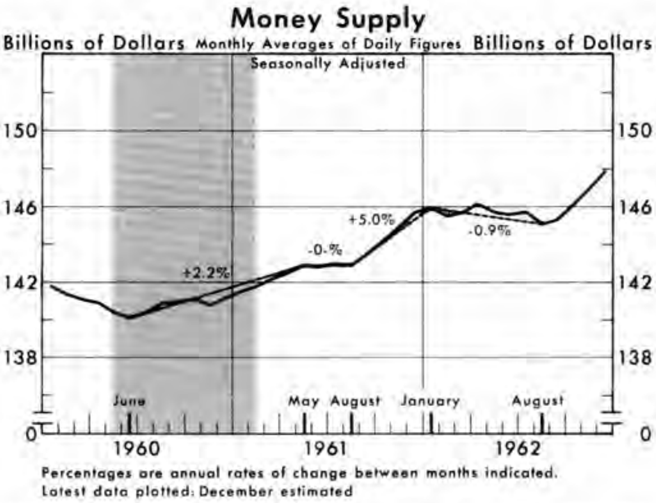
Open Market Operations

	Net Purchases (+) or Net Sales (—) Changes in Daily Average Figures (Millions of Dollars)	
	Unadjusted	Seasonally Adj.
January	$— 579	$— 13
February	— 135	+ 492
March	+ 186	+ 247
April	+ 573	+ 611
May	+ 360	+ 396
June	+ 65	— 237
July	+ 13	— 283
August	+ 507	+ 625
September	— 167	— 197
October	+ 320	+ 110
November	— 46	— 105
December	+ 351	— 240
Total	+1,448	

estate continued to rise sharply, and most other categories of loans shared to a lesser degree in the expansion. Bank investments increased slowly throughout the period from late 1961 to the end of 1962. In contrast, during previous postwar periods when loans have risen sharply, banks have usually reduced their holdings of securities in order to meet loan demands.

The Public's Liquidity

Trends in the money supply of the country paralleled the growth pattern in member bank reserves.



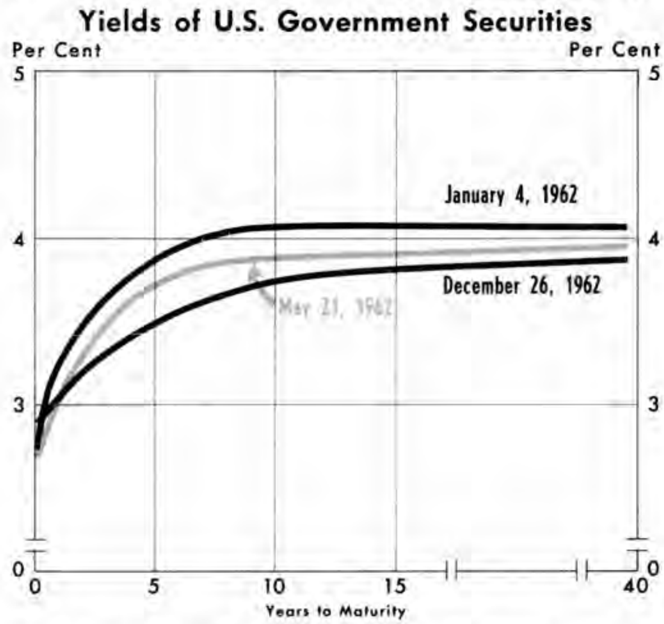
From May to August the money supply (demand deposits and currency) decreased slightly, but from August to the end of the year it rose sharply, at a rate of about 5 per cent per year. Time deposits and other liquid asset holdings of the public continued to expand rapidly during the last seven months of 1962. Money plus time deposits rose at an annual rate of 7 per cent during the May-December 1962 period.

Conclusions

At the outset of 1962, the United States economy was advancing and optimism was high that the two major economic problems, unemployment and a deficit in the country's balance of payments, would be ameliorated during the year. Much effort was devoted to reducing the adverse balance of payments through stimulating exports, reducing Government expenditures abroad, and other measures. Meanwhile, it was felt that short-term interest rates should be maintained since a decline would be likely to spark an outflow of short-term capital. An increase in bank reserves, bank credit, and the money supply was sought without permitting significant declines in short-term interest rates.

Many actions were taken by the Government to increase the liquidity of the country while minimizing downward interest rate pressures. An increase in the supply of short-term Treasury securities augmented the public's liquidity while maintaining short-term rates. Banks were supplied with reserves whenever short-term interest rates would not be pushed lower. In supplying reserves, the Reserve System made substantial open market purchases outside the short-term sector; in addition, reserve requirements on time deposits were reduced. The Treasury and the Federal Reserve System cooperated with other nations in smoothing potentially disruptive short-term foreign exchange disturbances.

Reflecting these efforts, short-term rates did not decline during 1962 but actually moved up slightly.

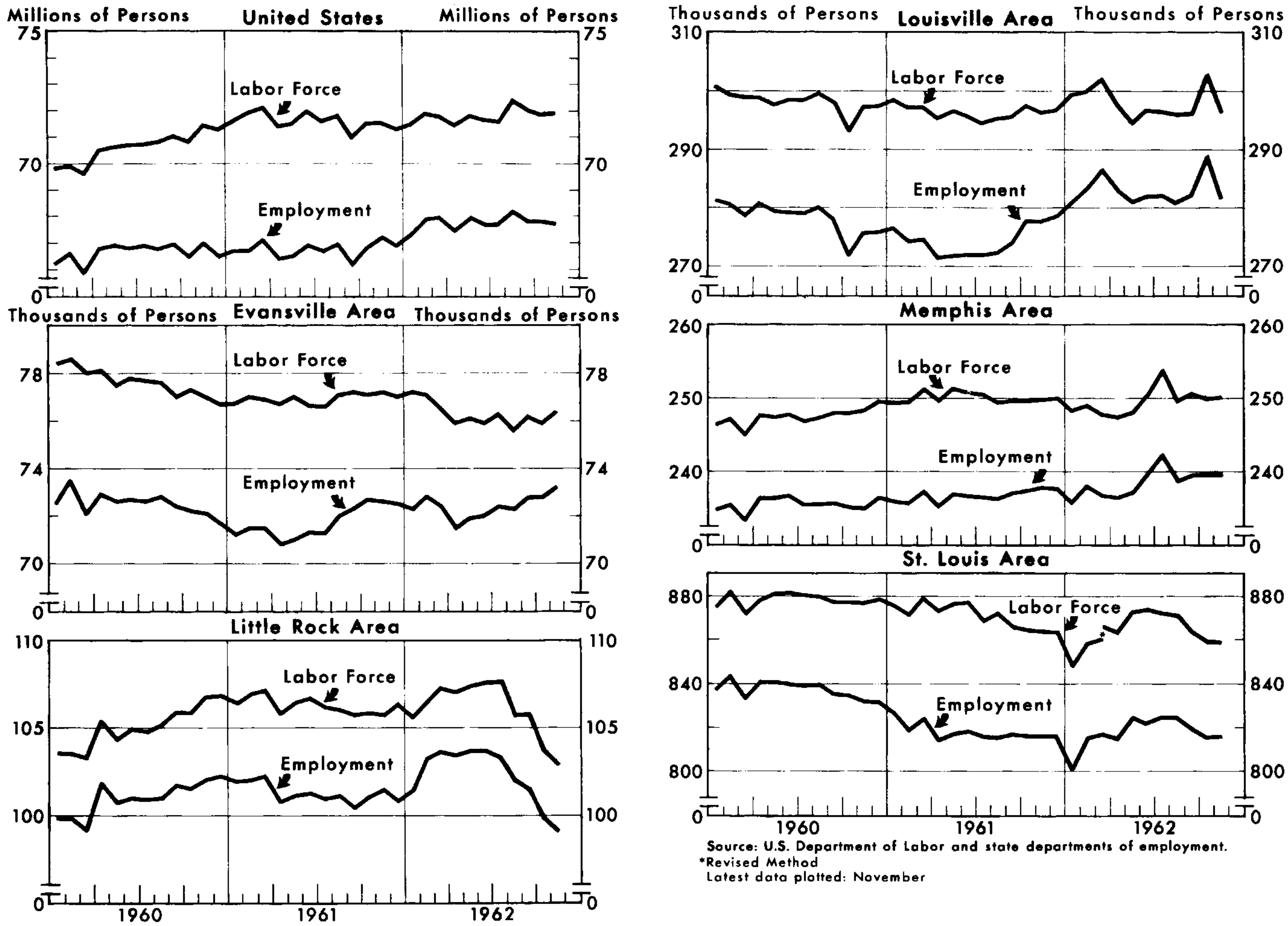


Most other interest rates drifted somewhat lower. Bank holdings of earning assets rose sharply and time deposits expanded at an annual rate of 18 per cent compared with 14 per cent in the previous year. Nevertheless, the limitations imposed by the interest rate guide kept monetary expansion relatively moderate during the year. Reserves available for private demand deposits were virtually unchanged during 1962, compared with a growth of 3.1 per cent in the previous year. The money supply of the country rose an estimated 1.5 per cent as against 3.2 per cent in 1961.

Early in 1962 there was an improvement in the nation's balance of payments. Domestic business activity expanded though at a progressively slower pace. After the second quarter the deficit in the balance of payments rose, and from the middle of 1962 to the end of the year business activity paused. At the year end, both the nation's balance of payments and the proportion of the country's resources that remained idle were little changed from a year earlier.

LABOR FORCE AND EMPLOYMENT –
PRINCIPAL DISTRICT LABOR MARKETS AND UNITED STATES

SEASONALLY ADJUSTED



Source: U.S. Department of Labor and state departments of employment.
*Revised Method
Latest data plotted: November

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