FORTY-EIGHTH

Annual Report

OF THE

BOARD OF GOVERNORS
of the Federal Reserve System

COVERING OPERATIONS FOR THE YEAR

1961

Digest of Principal Federal Reserve Policy Actions, 1961

Period	Action	Purpose of action
January	Limited net sales of U.S. Government securities from Federal Reserve portfolio to about $500 million. Member bank borrowing at Reserve Banks averaged only $50 million.	To encourage bank credit and monetary expansion by absorbing only part of seasonal inflow of reserve funds not otherwise offset by a large gold outflow.
February-August	Bought substantial amounts of U.S. Government securities with maturities over 1 year, following February 20 announcement that System open market operations would include securities outside the short-term area. These purchases were partly offset by net sales of short-term securities. Total System holdings of Governments increased about $700 million. Member bank borrowings averaged $75 million.	To encourage bank credit and monetary expansion while avoiding direct downward pressure on short-term interest rates, thereby moderating pressures on the U.S. balance of payments from outflow of short-term capital attracted by higher interest rates abroad.
September-December	Bought or sold at different times varying amounts of U.S. Government securities, including securities with longer maturities. Total System holdings of Government securities increased about $1.6 billion. Member bank borrowings at Reserve Banks remained generally low.	To continue to encourage bank credit and monetary expansion while allowing for changing reserve needs due to seasonal and other factors, including a large gold outflow, and while continuing to give consideration to the balance of payments problem.
December	Raised, effective Jan. 1, 1962, maximum interest rates payable by member banks on any savings deposit from 3 to 3½ per cent, and to 4 per cent on those left in the bank for 1 year or more; also raised maximum rates on time deposits with a maturity of 6 months to 1 year from 3 to 3½ per cent, and to 4 per cent on those deposits with a maturity of a year or longer.	To enable banks to compete more effectively for savings and other time deposits, including foreign time deposits, thus moderating pressures on the U.S. balance of payments, and, over the long run, to offer additional incentive for the accumulation of savings required for financing future economic growth.

continue to supply reserves only in the amounts that had been available in recent weeks would not be adequate to encourage or support credit and monetary expansion conducive to an early return to fuller utilization of human and material resources. He believed the risk that additional reserves might cause a decline in short-term rates and encourage a movement of funds from this country, with an accompanying loss of gold, was likely to be much less than it had been in the past.

2. Authority to effect transactions in intermediate- and longer-term securities.

The Federal Reserve Bank of New York was authorized, between this date and the next meeting of the Committee, within the terms and limitations of the directive issued at this meeting, to acquire intermediate- and/or longer-term U. S. Government securities of any maturity, or to change the holdings of such securities, in an amount not to exceed $500 million.

> Votes for this action: Messrs. Hayes, Balderston, Irons, King, Mills, Shepardson, Swan, and Wayne. Votes against this action: Messrs. Allen and Robertson.

Renewal of this special authorization, first granted on February 7, 1961, and amended on March 28 to permit operations in U. S. Government securities of all maturities, reflected the conclusion of the Committee that further operations outside the short-term market in pursuance of the objectives stated when the authorization was granted would be desirable. Messrs. Allen and Robertson dissented for reasons they had previously expressed.

May 9, 1961

1. Authority to effect transactions in System Account.

The Federal Open Market Committee made no change at this meeting in its policy directive providing that open market operations should be conducted with a view to encouraging expansion of bank credit and the money supply so as to contribute to

strengthening of the forces of recovery that appeared to be developing in the economy, while giving consideration to international factors.

> Votes for this action: Messrs. Hayes, Allen, Balderston, Irons, King, Mills, Robertson, Shepardson, Swan, and Wayne. Votes against this action: none.

From data presented at this meeting, economic recovery appeared to be proceeding more rapidly than had generally been anticipated, and at least as fast as the more optimistic forecasts had predicted it would. All available evidence pointed toward an increase in gross national product during the second quarter of the year. Preliminary data indicated that the Board's industrial production index for April would be up 3 points from the first quarter low of 102. In addition, schedules for steel and automobile production seemed virtually to assure some further rise in the index during May—perhaps enough to erase at least half of the 8-point decline from 110 in July 1960. Retail sales during April had been demonstrating strength, including sales of domestically produced automobiles, which had risen sharply in March from the depressed midwinter level. Dealer stocks of automobiles, which had been brought down somewhat in March from the relatively high levels that prevailed during the past year, had fallen further, and used car stocks were down sharply from a year earlier. Latest information regarding plant and equipment expenditure plans for 1961 indicated a decline of only 1 per cent from 1960, an improvement over indications of similar surveys made earlier in this year and in the fall of 1960. In the price area, consumer and wholesale prices generally had been stable, while sensitive commodities had moved up. On the other hand, in spite of the apparently growing strength of the economy, seasonally adjusted unemployment in April remained at about the midwinter high.

In the financial area, short-term interest rates declined somewhat in April and early May, while intermediate- and long-term rates showed marked declines except in the corporate market, where there had been an unusually large volume of new financing. Credit expansion continued during April and early May, but at only a moderate pace. The privately held money supply—defined as demand deposits and currency—increased moderately, the expansion seemingly stemming from an exceptionally large decrease in Treasury deposits. Owing to special factors, reserves were available to banks in somewhat larger volume during April than in March, despite a sizable reduction in the System portfolio, resulting in a somewhat easier tone in the money market than had been contemplated at the April 18 meeting of the Committee. Early in May, market factors absorbed some of these reserves.

The outflow of gold from the United States had virtually ceased during the past 2½ months, but private short-term capital movements outward had continued high during the first quarter of the year, and there was still an over-all deficit in the balance of payments, as conventionally measured, of about $1.5 billion (annual rate). The outflow of short-term capital continued despite a reduction in the differential between short-term rates in the United States and the higher rates available in most other important money markets.

In considering what policy should be followed until its next meeting, the Committee noted that, as mentioned previously, the tone of the money market during most of the period since the April 18 meeting was somewhat easier than had been contemplated at that meeting, largely because of unusual factors that included a high level of float. There was general recognition of the appropriateness of a policy of ease, but a majority felt that the ease had gone further than was desirable. As to interest rates, it was the majority view that it would be undesirable for the short-term rate to go lower, because of international considerations. Thus, the Committee renewed the existing directive without change, and the consensus was that operations for the System Account should be directed toward maintaining the same degree of ease that had prevailed in recent weeks, apart from the unusual ease that had developed during a portion of the period since the April 18 meeting.

Although all members voted to approve the Committee's directive without change, Messrs. Robertson and Swan dissented from the decision to implement the directive with operations aimed at the same degree of ease that had existed prior to the April 18 meeting rather than the greater degree of ease that had existed during most of the period since that date.

In dissenting, Mr. Robertson stated that it was his belief that the recent ease had promoted a turnaround in the money supply and brought about an increase in bank credit without unduly depressing yields on Government securities. The downswing in yields that had occurred was attributable more to the West German discount rate reduction and comments by persons outside the Federal Reserve System than to System open market operations. With the gold outflow apparently halted for the time being, and with inflationary pressures seemingly less dangerous just now than at any time in recent years, he believed that in order for the System to do its full part in stimulating recovery to more nearly satisfactory levels of production and employment, the degree of ease achieved during the past 3 weeks should not be diminished (and if anything, should be increased slightly) during the 4 weeks until the next meeting of the Committee.

Mr. Swan said that he dissented from the implementation of the directive with much more reluctance than at the previous two meetings. However, he saw no particular basis for change in the degree of ease actually achieved during the past 3 weeks and would continue a program of supplying reserves moderately in excess of seasonal needs to contribute to the expansion of bank credit and the money supply.

2. Authority to effect transactions in intermediate- and longer-term securities.

The Federal Reserve Bank of New York was authorized, between this date and the next meeting of the Committee, within the terms and limitations of the directive issued at this meeting, to acquire intermediate- and/or longer-term U. S. Government securities of any maturity, or to change the holdings of such securities, in an amount not to exceed $500 million.

Votes for this action: Messrs. Hayes, Balderston, Irons, King, Mills, Shepardson, Swan, and Wayne. Votes against this action: Messrs. Allen and Robertson.

The Committee in renewing this special authorization, first granted on February 7, 1961, and amended on March 28 to permit operations in U. S. Government securities of all maturities, concluded that further operations outside the short-term market in pursuing the objectives set forth in the directive would be desirable. Messrs. Allen and Robertson dissented for the same reasons they had stated previously.

June 6, 1961

1. Authority to effect transactions in System Account.

At this meeting, the Federal Open Market Committee, in directing that open market operations be with a view "to encouraging expansion of bank credit and the money supply so as to contribute to strengthening of the forces of recovery, while giving consideration to international factors," modified the wording of the preceding policy directive by deleting the phrase "that appear to be developing in the economy," qualifying words that had followed "the forces of recovery" in the directive that had been in effect since April 18, 1961.

Votes for this action: Messrs. Martin, Hayes, Allen, Balderston, Irons, King, Mills, Robertson, Shepardson, Swan, and Wayne. Votes against this action: none.

From data presented by the Committee members and the staff, it was apparent that the turning point of the recession had been reached quite some time earlier and that recovery had begun, although there was still doubt about the rate and probable duration of the business expansion. The few measures of economic activity available for May suggested that the pace of recovery had been maintained. Fragmentary data suggested that the Board's index of industrial production for May would be up 2 points from the preceding month, that retail trade figures would show a level well above first-quarter activity, and that employment measures would improve about seasonally for that

month. In the area of prices, broad measures of wholesale quotations had shown little change as scattered reductions offset increases in sensitive materials, and the consumer price index was unchanged from March to April, with the further likelihood that there would be little or no change from April to May.

The Committee observed that thus far the stimulus to the economy this year had come almost entirely from the reversal of inventory liquidation, the rise in Government expenditures, and the well maintained growth of consumption expenditures on nondurable goods and services. Neither trade reports nor surveys of buying intentions yet showed much evidence of a strong resurgence of demand for consumer durable goods or for housing, which had played such important roles in other postwar recoveries—a factor that caused misgivings in some quarters as to whether this recovery would carry forward after the initial stimulus of the inventory reversal disappeared.

Total loans and investments of banks increased substantially more than usual in May, reflecting largely bank participation in new Treasury financing. This bank credit expansion did not result in an increase in the seasonally adjusted private money supply, defined as demand deposits and currency outside of banks; but there were large increases in time deposits and U. S. Treasury deposits. Interest rates, which early in May had declined to the lowest levels since 1958, had since risen close to, and in some cases above, the highs that had been reached at times during the past 10 months. Short-term rates in particular had been influenced lately by a less marked degree of ease than prevailed shortly before the May 9 meeting, by prospective Treasury financing in the short-term area, and by the approach of the mid-June tax date, which date generally is preceded by reduced nonbank demand for Treasury bills. In addition, the demand on capital markets had been large and seemed likely to continue fairly heavy.

While the U. S. balance of payments position had shown considerable improvement compared with the fourth quarter of 1960, the current close balance in U. S. accounts was considered