

FIFTY-FIRST

Annual Report

OF THE

BOARD OF GOVERNORS
of the Federal Reserve System



COVERING OPERATIONS FOR THE YEAR

1964

DIGEST OF PRINCIPAL FEDERAL RESERVE POLICY ACTIONS IN 1964

| Period | Action | Purpose |
|------------------------------|---|--|
| January– mid-August | Increased the System's holdings of U.S. Government securities, after having reduced them seasonally early in the year. On balance, total holdings rose about \$1.1 billion, \$300 million of which represented net purchases of securities with maturities of over 1 year. Member bank borrowings averaged about \$275 million. | To provide for moderate growth in the reserve base, bank credit, and the money supply for the purpose of facilitating continued expansion of the economy while fostering improvement in the capital account of U.S. international payments, after offsetting seasonal downward pressures on short-term interest rates early in the period. |
| Mid-August– late November | Increased the System's holdings of U.S. Government securities by about \$1.5 billion, of which \$600 million represented net purchases of securities with maturities of more than 1 year. Member bank borrowings averaged about \$350 million. | To maintain slightly firmer conditions in the money market with a view to minimizing the outflow of funds attracted by higher short-term interest rates abroad while offsetting reserve drains and providing for growth needs of the domestic economy. |
| Late November | Raised discount rates from 3½ to 4 per cent. Raised maximum interest rates payable on savings deposits held for less than 1 year from 3½ to 4 per cent and those on other time deposits from 4 to 4½ per cent for maturities of 90 days or more and from 1 to 4 per cent for maturities of 30-89 days. | To counter possible capital outflows that might be prompted by any widening spread between money market rates in this country and the higher rates abroad, following a rise in official and market rates in London, while at the same time ensuring that the flow of savings to commercial banks remains ample for the financing of domestic investment. |
| Late November– December | Increased the System's holdings of U.S. Government securities by about \$765 million, part of which represented securities acquired under repurchase agreements. Member bank borrowings averaged about \$275 million. | To offset seasonal reserve drains and to accommodate further moderate expansion in aggregate bank reserves while ensuring that the rise in money market rates following the discount rate actions did not restrict the availability of domestic credit. |

to 7 per cent in another of a series of actions taken in response to heavy pressure on sterling in foreign exchange markets.¹ At this meeting the Special Manager of the System Account reported that pressure on sterling had abated for only a brief period following this action, and had subsequently been renewed in force. He indicated that a number of central banks were consulting regarding the possibility of developing a broad package of financial assistance to Britain, designed to reinforce that country's efforts to defend sterling. On recommendation of the Special Manager, the Committee authorized an increase in the reciprocal currency (swap) arrangement with the Bank of England from \$500 million to \$750 million, subject to the agreement of the Bank of England and to the satisfactory development of a broad package of credits to Britain.

Concurrently, the Committee raised the dollar limit specified in the first paragraph of the continuing authority directive for foreign currency transactions on the aggregate amount of foreign currencies held under reciprocal currency arrangements by \$250 million to \$2.35 billion.

Votes for this action: Messrs. Martin, Hayes, Balderston, Daane, Hickman, Mills, Robertson, Shepardson, Shuford, Swan, and Wayne. Votes against this action: None.

December 1, 1964

Authority to effect transactions in System Account.

Domestic financial markets had reacted in a moderate and orderly fashion to the preceding week's official actions, which

¹ As indicated in the entry for Nov. 23, 1964, in the preceding Record of Policy Actions of the Board of Governors, on the same date the Board approved increases in Federal Reserve discount rates from 3½ to 4 per cent and amended the Supplement to Regulation Q to raise maximum permissible interest rates on time and savings deposits of member banks.

followed the sterling crisis. These actions included successive increases in discount rates by the Bank of England, the Federal Reserve Banks, and the Bank of Canada; an increase in the maximum interest rates permitted on time and savings deposits of member banks under the Federal Reserve Board's Regulation Q; and announcement of a \$3 billion package of short-term credits to Britain by 11 countries, including the United States, and the Bank for International Settlements.

Interest rates, particularly on short-term instruments, adjusted upward promptly in response to the official rate actions. Yields on 3-month Treasury bills advanced about 25 basis points to about 3.85 per cent, and Federal funds frequently traded at the new Federal Reserve discount rate of 4 per cent. The rise in bond yields, however, was quite modest; yields on long-term Treasury issues advanced about 5 basis points on the average, and those on outstanding corporate and municipal bonds appeared to have adjusted to about the same extent. Common stock prices dropped only slightly on somewhat heavier trading volume, and neither spot nor futures markets for sensitive commodities showed unusual changes in price quotations or activity. A number of commercial banks raised rates offered on time and savings deposits, but announcements of increases in prime lending rates by a few banks (all outside New York) were not followed immediately by others.

From reports at this meeting it appeared that the domestic business situation had remained strong in recent weeks, although current measures of activity continued to reflect the effects of recent and threatened work stoppages. Retail sales declined by about 3 per cent in October and somewhat further in early November, both because of a shortage of new cars resulting from the recent auto industry strikes and because of unseasonably warm weather. Industrial production was estimated to have returned in November to about the September level as auto output was partly restored and as production in other industries

continued to increase. Manufacturers' inventories rose by \$550 million in October, more than in any other month thus far in 1964. However, this development also probably was related in part to work stoppages; automobile manufacturers accumulated stocks of materials and parts during the auto strikes and steel users increased inventories against the possibility of a strike in that industry next spring.

Between mid-September and mid-October the index of industrial commodity prices increased by 0.4 per cent to a level above the narrow range within which it had fluctuated earlier this year. The rise was attributable to a recovery in prices of petroleum products, further advances for nonferrous metals, and scattered increases in other commodity groups. Few decreases were recorded other than slight further declines for lumber and plywood.

Bank credit, which had declined in October, rose substantially in November according to data for city banks, as business and financial loans increased and banks acquired sizable amounts of U.S. Government securities offered in Treasury financings. Most of the associated rise in deposits apparently occurred in Government and time deposits, and the money supply probably increased only slightly in November. In the August-October period, bank credit had grown at an annual rate of about 10 per cent, and the money supply at a rate slightly less than 5 per cent. Free reserves, the data for which were affected more sharply than usual by subsequent revisions, averaged about \$10 million in November, compared with an average of about \$90 million in the previous month.

Data on the U.S. balance of payments for October and tentative figures for early November suggested that the deficit in the fourth quarter would be somewhat higher than in the third, partly because of a substantial increase in new foreign security issues in the United States. It appeared that the large recent outflow of capital from Britain would not greatly affect the statistics for the U.S. payments deficit.

In the discussion of the appropriate monetary policy for the

next 2 weeks, it was noted that financial markets were still in process of adjustment to recent official actions and that these markets would be under strong seasonal pressures in the period ahead. It also was noted that the Federal Reserve rate actions had been directed primarily to the international payments situation, and that they had been intended to reduce the possibility of an outflow of volatile foreign dollar balances for confidence reasons. The Committee agreed that it was desirable at present to avoid a reduction in domestic credit availability and to moderate firming tendencies in the money market.

The following current economic policy directive was issued to the Federal Reserve Bank of New York:

It is the Federal Open Market Committee's current policy to accommodate moderate growth in the reserve base, bank credit, and the money supply for the purpose of facilitating continued expansion of the economy, while fostering improvement in the capital account of U.S. international payments, and seeking to avoid the emergence of inflationary pressures. This policy takes into account the fact that financial markets are currently in a period of adjustment in the wake of the recent sterling crisis and the discount rate advances and other responses in Britain, Canada, and the United States. The policy also takes into account the underlying strength of the domestic economy, obscured partially by the effects of recent and threatened work stoppages; the recent increase in average wholesale prices of industrial goods; and the continued expansion of bank credit and money. It also gives consideration to the persistence of a sizable deficit in the U.S. balance of payments.

To implement this policy, and recognizing that a larger-than-usual degree of flexibility in operations will be needed in this period when financial markets, while under strong seasonal pressures, are still adjusting to official rate actions here and abroad, System open market operations over the next 2 weeks shall be conducted with a view to accommodating moderate expansion in aggregate bank reserves, while moderating adjustments of money market conditions to recent official actions.

Votes for this action: Messrs. Martin, Hayes, Balderston, Hickman, Mitchell, Robertson, Shepardon, Shuford, Swan, and Wayne. Votes against this action: None.