FORTY-NINTH

Annual Report

OF THE

BOARD OF GOVERNORS
of the Federal Reserve System

COVERING OPERATIONS FOR THE YEAR

1962

Period	*Action*	*Purpose of action*
January-February	Reduced System holdings of U. S. Government securities by about $500 million through net sales and redemptions. Member bank borrowings from the Reserve Banks averaged less than $100 million.	To permit further bank credit and monetary expansion by absorbing only part of seasonal inflow of reserve funds, mainly from post-holiday return of currency from circulation, while minimizing downward pressures on short-term interest rates.
February	Authorized open market transactions in foreign currencies.	To moderate and offset short-term pressures on the dollar in the foreign exchange market.
March-mid-June	Increased System holdings of U. S. Government securities by about $1.3 billion, of which half represented purchases of securities with maturities of more than 1 year. Member bank borrowings from Reserve Banks continued to average less than $100 million.	To promote further bank credit and monetary expansion while avoiding sustained downward pressures on short-term interest rates.
Mid-June-late October	Increased System holdings of U. S. Government securities by about $200 million with net sales and redemptions of Treasury bills of about $700 million being more than offset by purchases of coupon issues, of which two-thirds were issues maturing in more than 1 year. Member bank borrowings from Reserve Banks averaged less than $100 million.	To permit moderate increase in bank credit and money supply while avoiding redundant bank reserves that would encourage capital outflows, taking into account gradual improvement in domestic economy and possibilities for further advance, while recognizing the bank credit growth of past year and continuing adverse balance of payments.
July	Reduced margin requirements on loans for purchasing or carrying listed securities from 70 to 50 per cent of market value of securities.	To take into account the recent sharp reduction in stock market credit and the abatement in speculative psychology in the stock market.
October	Reduced reserve requirements against time deposits from 5 to 4 per cent, effective October 25 for reserve city banks and November 1 for other member banks, thereby releasing about $780 million of reserves.	To help meet seasonal needs for reserves, while minimizing downward pressures on short-term interest rates, and to provide for the longer-term growth in bank deposits needed to facilitate the expansion in economic activity and trade.
Late October-December	Increased System holdings of U. S. Government securities by about $1.0 billion, with more than half of the net increase in issues maturing in more than 1 year. Member bank borrowing from the Reserve Banks rose gradually over period, but only to an average of about $200 million.	To help further in meeting seasonal needs for reserve funds while encouraging moderate further increase in bank credit and the money supply and avoiding money market conditions unduly favorable to capital outflows internationally. In mid-December open market operations were modified to provide a somewhat firmer tone in money markets and to offset the anticipated seasonal easing in Treasury bill rates.

January data (the latest available), was running below both the fourth quarter and the first quarter of 1961.

The outflow of gold approximated $300 million in the current quarter, although some part of that amount might be viewed as offset by an increase in U.S. holdings of foreign convertible currencies. Reductions in the United Kingdom bank rate suggested a decrease in British interest-rate levels, but it was not clear whether or to what extent funds hitherto attracted to the United Kingdom would flow to New York.

Differences among Committee members with respect to the type of policy called for by these developments were generally small. Most members felt that the balance of payments situation continued to call for a domestic interest-rate structure that would not encourage outflows of funds, and thus were concerned about the declining tendency in interest rates. This tendency, it was noted, might well be accentuated by continuing to provide reserve availability to facilitate expansion in bank credit domestically, which most members also regarded as desirable. Some of the members, having in mind the modest nature of the expansion in domestic activity, were inclined to ease slightly. A few members, in fact, would have preferred taking more decisive easing action, but one member recommended a policy of less ease. The majority, however, concluded that on balance no significant change in policy should be made. The two changes made in the wording of the current economic policy directive were intended to make clear that the general policy in effect in the preceding period and now being continued was designed to effect slightly more expansion in reserve availability than had actually developed. The policy directive issued to the Federal Reserve Bank of New York read as follows:

In view of the modest nature of recent advances in the pace of economic activity and the continued underutilization of resources, it remains the current policy of the Federal Open Market Committee to promote further expansion of bank credit and the money supply, while giving recognition to the country's adverse balance of payments and the need to maintain a viable international payments system.

To implement this policy, operations for the System Open Market Account during the next 3 weeks shall be conducted with a view to maintaining a supply of reserves adequate for further credit and monetary expansion, taking account of the desirability of avoiding sustained downward pressures on short-term interest rates.

Votes for this action: Messrs. Martin, Balderston, Bryan, Ellis, Mitchell, Robertson, Shepardson, Clay, Scanlon, and Treiber. Vote against this action: Mr. Mills.

Mr. Mills dissented on the ground that the long maintained high level of free reserves had forced excessive liquidity into the economy and thereby had laid the foundation for future inflationary difficulties. Moreover, he felt that monetary policy by its declared purpose of holding interest rates on Treasury bills at a level intended to deter transfer of funds abroad had set a floor under bill rates and, in his opinion, had encouraged speculative operations in all maturities of U.S. Government securities. Mr. Mills felt that these and other difficulties could have been avoided by policy objectives geared solely to providing adequate credit availability—an amount that would have resulted in a somewhat firmer interest-rate structure but which still would have permitted sufficient bank credit expansion. He believed that the assumption that there must be close coordination between growth in the money supply and growth in gross national product was erroneous, and monetary policy should pay close attention to encouraging constructive commercial bank lending and investing practices.

April 17, 1962

Authority to effect transactions in System Account.

Information regarding developments in the domestic economy that had become available in the period since the preceding meeting of the Committee provided some definite signs of improvement. However, uncertainties remained about the course of developments in a number of strategic areas, such as residential and other construction, consumer durable goods other than autos, and business investment in new plant and equipment. For residential building, March statistics on the number of housing units started had not yet become available, but starts in February had shown a further decline to a relatively low level.

The Board's industrial production index was reported to have risen 1 point further in March to a new high of 116 per cent of the 1957 average. Nonagricultural employment and the length of the factory workweek also increased in March, and the rate of unemployment edged down from 5.6 per cent to 5.5 per cent of the civilian labor force. The labor force, however, was no higher than a year earlier, and resumption of normal growth in the labor force in the near future might limit declines in unemployment even under conditions of expanding employment. Sales of new autos had picked up considerably in March and early April, and sales at department stores also had risen.

Commodity prices had continued to show little change in the weeks immediately preceding this meeting. Announcement of the recision of the rise in steel prices served to reduce whatever expectations there might otherwise have been of imminent upward general price changes, but the view was expressed that this action might have added to uncertainties of a different sort. Stock market prices had declined in early April, while markets for fixed-income securities had continued strong.

Bank reserves available as backing for private deposit expansion and total bank credit had both increased more than seasonally since the March 27 Committee meeting. Free reserves in the past 3 weeks had averaged moderately higher than in the preceding period, while total reserves and required reserves had increased substantially after a sluggish performance in February and March. Time deposits at banks continued to increase sharply, and available information indicated that savings in other financial institutions had also continued to increase. Demand deposits had moved upward, following several weeks of little change, and the seasonally adjusted money supply was indicated to have risen in the first half of April.

Yields on 3-month Treasury bills continued to fluctuate in a narrow range as increased demands in credit markets and additions to weekly bill offerings counteracted a steady investor demand for short-term securities. Federal funds remained in the 2¾ to 3 per cent range. Yields on longer-term Treasury issues declined further. Despite a large volume of new financing in March and a prospectively larger volume in April, yields on corporate and municipal bonds continued at the low levels reached earlier or declined further. Mortgage rates also drifted down further.

The balance of payments situation in March, and fragmentary indications for early April, suggested little or no improvement. The March deficit was estimated at $360 million, including net gold sales of $150 million, and was higher than for January and February combined. The trade surplus in February had been quite large, with exports at a record annual rate of nearly $22 billion and imports continuing at $15.75 billion. The rate of outflow of capital remained large in March but was smaller than in the final quarter of 1961. There was in prospect a heavy calendar of foreign security issues in the U.S. market.

The majority of the Committee members agreed, although with some differences of interpretation and emphasis, that no change was indicated at this time in monetary and credit policy or in the wording of the current directive, particularly in view of the imminence of a substantial Treasury financing program. As a result, the Committee issued a current economic policy directive to the Federal Reserve Bank of New York in the same form as the directive issued at the meeting on March 27, 1962.

Votes for this action: Messrs. Martin, Balderston, Bryan, Deming, Ellis, Fulton, King, Mills, Mitchell, Robertson, and Shepardson. Vote against this action: Mr. Hayes.

Mr. Hayes dissented because he felt that the degree of liquidity of the economy, coupled with recent signs of a somewhat improved rate of business expansion, would warrant placing a little more emphasis on the troublesome international aspects of the country's current economic problems. He noted that the country's ability to withstand heavy balance of payments deficits and accompanying gold drains was not unlimited and that he had yet to see any convincing evidence of a real turn in the tide. He expressed particular concern about the volume and breadth of foreign borrowing in the United States, both from banks and through bond offerings. In these circumstances, he felt that the System should edge toward a moderately less easy reserve position, thus encouraging the development of a somewhat higher structure of interest rates, particularly short-term rates.

Another member of the Committee (Mr. Mills) continued of the view he had expressed at previous meetings that a firming of policy was indicated. At the moment, however, he felt that the imminent Treasury financing precluded policy changes such as he had advocated.

May 8, 1962

Authority to effect transactions in System Account.

The economy had continued to register moderate gains in over-all activity, with little change in commodity prices. One factor of significant improvement was a sharp rise in March in the number of new housing units started, following 4 months of decline of much more than seasonal proportions. Another was the expansion of business plans for fixed capital outlays, as reported by a recent survey. This survey indicated a prospective rise in such outlays of 11 per cent for 1962, as compared with a rise of 8 per cent reported by a different survey taken several weeks earlier. Although data had not yet become available for total retail sales and industrial production in April, incomplete weekly and other information suggested moderate further advances. There was no significant change in the rate of unemployment.

Less favorable to economic prospects were the early indications of corporate profits for the first quarter. Although substantially above year-earlier levels, such profits had apparently failed to hold the rise achieved in the fourth quarter of 1961. Also, the volume of new orders received by durable goods producers had declined somewhat further in March from the advanced level reached at the beginning of the year. Stock market prices continued to decline.

Bank reserves available to support private deposit expansion had risen more than seasonally in April. Excess reserves had increased, while the small amount of member bank borrowing had been further reduced. Free reserves averaged moderately higher than in March. Total bank loans and investments rose again in April, with the sharpest increase in bank holdings of securities other than U.S. Governments. Both total and business loans had shown moderate strength.

The seasonally adjusted money supply, which increased somewhat in March, rose substantially further in April. Time and savings deposits at commercial banks had continued to rise, but at a somewhat less rapid pace than in other recent months.

Capital market financing had accelerated in April, and new corporate issues were substantially above the first-quarter average. Municipal issues held at the relatively high first-quarter average. Both corporate and municipal issues were expected to be in smaller volume in May.

Money markets had been generally steady in the 3 weeks preceding the meeting. Federal funds were traded in the 2½-3 per cent range, with the bulk of the trading at 2¾ per cent. Yields on U.S. Government securities had been unusually stable, while yields on corporate and municipal bonds had continued to edge lower.

In the first quarter of 1962, the U.S. balance of payments position was far more favorable than in the preceding quarter (partly reflecting seasonal factors), but less favorable than in the first quarter of 1961. The balance of payments deficit dropped sharply between March and April, but some of the improvement