

FIFTIETH
Annual Report

OF THE
BOARD OF GOVERNORS
of the Federal Reserve System



COVERING OPERATIONS FOR THE YEAR

1963

<i>Period</i>	<i>Description</i>	<i>Purpose</i>
January- mid-May	Reduced System holdings of U.S. Government securities and then increased them in line with seasonal and moderate growth needs of the economy. Total holdings rose about \$470 million on balance, owing mainly to net purchases of issues maturing in more than 1 year. Member bank borrowing rose slightly to a level of about \$150 million in the first half of May.	To offset seasonal downward pressures on short-term interest rates early in the period and to provide for growth in bank credit and the money supply at a rate consistent with minimizing capital outflows in accordance with the policy of slightly reduced reserve availability adopted at the December 18, 1962, meeting of the Federal Open Market Committee.
Mid-May- late-July	Reduced the degree of reserve availability slightly further. System holdings of U.S. Government securities increased nearly \$1.2 billion, about one-fifth representing net purchases of issues maturing in more than 1 year. Member bank borrowing increased further, averaging \$275 million over the period.	To achieve a slightly greater degree of firmness in the money market in order to minimize the outflow of capital while continuing to provide reserves for moderate monetary and credit growth.
Mid-July	Raised the discount rate from 3 to 3½ per cent. Raised maximum interest rates payable by member banks on time deposits (other than savings) and certificates of deposit with maturities of 90 days to 6 months from 2½ to 4 per cent and with maturities of 6 months to 1 year from 3½ to 4 per cent.	To help reduce short-term capital outflows by firming U.S. short-term money market rates and permitting member banks to compete more effectively for foreign and domestic funds.
Late-July- December	Reduced a little further the degree of reserve availability. System holdings of U.S. Government securities increased about \$1.1 billion, of which more than one-half represented purchases of securities with maturities of more than 1 year. Member bank borrowing averaged about \$325 million over the period.	To attain slightly more firmness in the money market, in the context of a higher discount rate, with a view to minimizing the outflow of funds abroad while offsetting seasonal reserve drains and providing for growth needs of the domestic economy.
November	Raised margin requirements on loans for purchasing or carrying listed securities from 50 to 70 per cent of market value of securities. Also increased retention requirements on proceeds of sales from undermargined accounts from 50 to 70 per cent.	To help prevent excessive use of stock market credit, which had increased sharply since July 1962, when margin requirements were lowered from 70 to 50 per cent.

and the United States were subject to reversals in direction, and, more generally, because the reciprocal currency arrangements were best viewed as a mutual defense under which short-term credit would be extended by either party when required by the other.

In a related action the Committee modified the amounts and form of the dollar limitations specified in the continuing authority directive for System foreign currency operations. In place of the previous limit of \$1.75 billion on total foreign currency holdings at any one time, two separate limits were specified: a limit of \$1.95 billion on foreign currencies held under reciprocal currency arrangements, and a limit of \$150 million on foreign currencies held as a result of outright purchase. The former figure was equal to the sum of the amounts currently specified by the Committee for all individual authorized reciprocal currency arrangements, and therefore represented the maximum of System covered holdings of foreign currencies under these arrangements, in the remote possibility that they might all simultaneously be fully drawn on. The limit of \$150 million on forward transactions that had been previously specified was retained.

Reflecting these actions, the directive issued to the Federal Reserve Bank of New York read as follows:

The Federal Reserve Bank of New York is authorized and directed to purchase and sell through spot transactions any or all of the following currencies in accordance with the Guidelines on System Foreign Currency Operations reaffirmed by the Federal Open Market Committee on March 5, 1963, as amended May 28, 1963; provided that the aggregate amount of foreign currencies held under reciprocal currency arrangements shall not exceed \$1.95 billion equivalent at any one time, and provided further that the aggregate amount of foreign currencies held as a result of outright purchases shall not exceed \$150 million equivalent at any one time:

Pounds sterling
French francs
German marks
Italian lire
Netherlands guilders

Swiss francs
Belgian francs
Canadian dollars
Austrian schillings
Swedish kronor
Japanese yen

The Federal Reserve Bank of New York is also authorized and directed to operate in any or all of the foregoing currencies in accordance with the Guidelines and up to a combined total of \$150 equivalent, by means of:

- (a) purchases through forward transactions, for the purpose of allowing greater flexibility in covering commitments under reciprocal currency agreements;
- (b) purchases and sales through forward as well as spot transactions, for the purpose of utilizing its holdings of one currency for the settlement of commitments denominated in other currencies; and
- (c) purchases through spot transactions and sales through forward transactions, for the purpose of restraining short-term outflows of funds induced by arbitrage considerations.

Votes for this action: Messrs. Martin, Hayes, Balderston, Bopp, Clay, Mills, Mitchell, Robertson, Scanlon, Shepardson, and Shuford. Votes against this action: None.

Messrs. Mills and Mitchell voted favorably on this directive despite their opposition to a reciprocal currency arrangement with the Bank of Japan because the Committee earlier had approved negotiation of such an arrangement in an action to which their dissents were already recorded.

November 12, 1963

1. Authority to effect transactions in System Account.

Information available for October indicated a pick-up in domestic economic activity and broad stability in price indexes, but a continued high rate of unemployment. Industrial production was estimated at or fractionally above the September level,

and retail sales had risen to a new high, with automobile markets especially strong. Construction activity continued steady at a level about 5 per cent above a year earlier.

Business sentiment appeared more optimistic than earlier. A private survey of business plans for 1964, released November 8, indicated an increase of 4 per cent in fixed capital outlays relative to 1963. In past business expansions this survey had tended to underestimate the amount of change actually realized.

Seasonally adjusted commercial bank credit expanded only moderately further in October, and growth so far this year had been somewhat slower than in the corresponding period of 1963. Business loan demand again was strong, and banks continued to make substantial sales of U.S. Government securities.

The private money supply, seasonally adjusted, increased substantially further in October. The rise was associated with an unusually large decline in U.S. Government deposits at commercial banks. Time and savings deposits also increased at a rate somewhat greater than in other recent months.

Stock market prices declined moderately in early November, after reaching new highs in late October. The October rise was associated with a large trading volume and a further increase in stock market credit. Effective November 6, the Board of Governors increased margin requirements from 50 per cent to 70 per cent.

Corporate and municipal financing increased sharply in October from the moderate volume of preceding months, but was expected to drop back in November. Yields on U.S. Government securities continued to rise and except for the longest maturities were at their highest levels since the spring of 1960. Rates on 3-month Treasury bills recently had moved above the 3½ per cent discount rate and prior to this meeting were 3.55 per cent. These rate increases were attributable to a combination of factors: a large volume of short-term issues by the Treasury in the last 10 days of October; continued bank liquidation of Government securities; increased optimism about the

business outlook; and an expectation, widely held in financial markets, that money market conditions might soon become somewhat firmer.

The third-quarter international payments deficit, sharply reduced from the second quarter by declines in direct investment, in new foreign security issues, and in outflows of short-term money market funds, was estimated at a seasonally adjusted annual rate of about \$2 billion. (This estimate excluded the effects of special Government transactions and of the July reflux of window-dressing credits.) Abroad, activity was continuing to expand, but it seemed possible that limited availability of manpower and other resources in several major European countries in the face of expanding demands might result in slower rates of real growth, stronger inflationary trends, and more restrictive monetary policies in those countries.

The Committee believed that circumstances did not warrant a change in monetary policy at this time and agreed that over the next 3 weeks reserves should be supplied to accommodate the expected seasonal expansion in demand for bank credit.

Within this consensus, however, several members expressed concern about the recent increases in short-term interest rates, especially the rise in the rate on 3-month Treasury bills to a level somewhat above the discount rate. They felt that these increases were undesirable because they reinforced market expectations of imminent discount rate action and, if continued, would contribute to upward pressures on both domestic longer-term yields and interest rates abroad. Some other members felt that the recent increases in short-term rates and the firming of other credit market indicators were appropriate in view of the substantial recent expansion of the reserve base and the high level of liquidity in the economy. They expressed the view that a firmer policy posture might be warranted in the near future.

The current economic policy directive issued to the Federal Reserve Bank of New York differed from the one adopted at the previous meeting of the Committee only by deletion of a

reference, no longer applicable, to Treasury financing. It read as follows:

It is the Federal Open Market Committee's current policy to accommodate moderate growth in bank credit, while maintaining conditions in the money market that would contribute to continued improvement in the capital account of the U.S. balance of payments. This policy takes into consideration the fact that domestic economic activity is expanding further, although with a margin of underutilized resources; and the fact that the balance of payments position is still adverse despite a tendency to reduced deficits. It also recognizes the increases in bank credit, money supply, and the reserve base of recent months.

To implement this policy, System open market operations shall be conducted with a view to maintaining the degree of firmness in the money market that has prevailed in recent weeks, while accommodating moderate expansion in aggregate bank reserves.

Votes for this action: Messrs. Martin, Hayes, Balderston, Bopp, Clay, Irons, Mitchell, Robertson, Scanlon, and Shepardson. Vote against this action: Mr. Mills.

Mr. Mills dissented because he felt that present policy was undesirably restrictive for viability of the domestic economy. He thought that measures required to combat any further balance of payments difficulties should be taken in the area of fiscal controls, and he favored increasing the supply of reserves to relieve some of the existing upward pressure on interest rates and to reduce what he considered to be a threat to appropriate growth in the money supply.

2. Amendment of continuing authority directive.

In accordance with a suggestion of the Account Manager, Section 1(a) of the continuing authority directive to the Federal Reserve Bank of New York was amended to reduce the limit on net changes in the System Open Market Account in any period between meetings of the Committee to \$1 billion from the \$1.5 billion that had been established at the meeting on October 1. Earlier in the year the limit had been \$1 billion,

except for the period between the meetings of June 18 and July 30, when it was \$1.5 billion.

Votes for this action: Messrs. Martin, Hayes, Balderston, Bopp, Clay, Irons, Mills, Mitchell, Robertson, Scanlon, and Shepardson. Votes against this action: None.

3. Authority to purchase and sell foreign currencies.

Since early September the U.S. Stabilization Fund had been engaged in a program of spot purchases of Italian lire for two purposes: to help the Italian authorities cushion the abrupt decline that had been occurring in their monetary reserves, and to accumulate funds for repayment of the Treasury's bonded debt denominated in lire and maturing over the period from March 1964 to September 1965. However, the resources of the Stabilization Fund for this type of operation were limited. The Special Manager of the System Account recommended that the Federal Reserve Bank of New York be authorized to make spot purchases of Italian lire, at a rate above par if necessary, for purposes of immediate forward sale to the Treasury at the same rate, in order to assist in achieving the two objectives underlying recent Treasury lire purchases. He also recommended that authority be granted to conduct similar operations in other foreign currencies in which the Treasury had outstanding indebtedness to facilitate Treasury repayment of these debts. The Committee concluded that such operations appeared sufficiently likely to be useful to warrant their approval on an experimental basis, and the continuing authority directive for System foreign currency operations was amended by the addition of the following paragraph:

The Federal Reserve Bank of New York is also authorized and directed to make purchases through spot transactions, including purchases from the U.S. Stabilization Fund, and concurrent sales through forward transactions to the U.S. Stabilization Fund, of any of the foregoing currencies in which the U.S. Treasury has outstanding indebtedness, in accordance

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with the Guidelines and up to a total of \$100 million equivalent. Purchases may be at rates above par, and both purchases and sales are to be made at the same rates.

Votes for this action: Messrs. Martin, Hayes, Balderston, Bopp, Clay, Irons, Mills, Mitchell, Robertson, Scanlon, and Shepardson. **Votes against this action:** None.

November 26, 1963

Authority to effect transactions in System Account.

This meeting was held by telephone on the first business day following the death of President Kennedy. It was called for the purpose of considering whether action by the Committee was required to deal with any actual or potential unsettlement in domestic financial markets or in foreign exchange markets stemming from the President's death.

Reports by the Manager and the Special Manager of the System Open Market Account indicated that there was no evidence of adverse market developments as of late morning. The Account Manager reported that the Government securities market had opened with a confident tone, and that prices at the opening were unchanged or slightly higher on securities of various maturities. The stock market already had made a good recovery in early trading. The Special Manager noted that gold and foreign exchange markets were steady, and that where necessary central banks were acting to maintain foreign exchange rates at their previous levels.

The Committee decided that it was desirable, as a precautionary measure, to revise its current economic policy directive in order to insure that the Federal Reserve Bank of New York would have ample authority to deal with any unsettlement that might develop. The revision was confined to the second paragraph, and the directive was issued in the following form:

It is the Federal Open Market Committee's current policy to accom-

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moderate moderate growth in bank credit, while maintaining conditions in the money market that would contribute to continued improvement in the capital account of the U.S. balance of payments. This policy takes into consideration the fact that domestic economic activity is expanding further, although with a margin of underutilized resources; and the fact that the balance of payments position is still adverse despite a tendency to reduced deficits. It also recognizes the increases in bank credit, money supply, and the reserve base of recent months.

To implement this policy, System open market operations shall be conducted with a view to cushioning any unsettlement that might arise in money markets stemming from the death of President Kennedy and to maintaining about the same conditions in the money market as have prevailed in recent weeks, while accommodating moderate expansion in aggregate bank reserves.

Votes for this action: Messrs. Martin, Hayes, Balderston, Bopp, Clay, Irons, Mitchell, Robertson, Scanlon, and Shepardson. **Vote against this action:** Mr. Mills.

Mr. Mills dissented for the same reasons he had dissented from the directive adopted at the meeting of November 12, 1963; he thought the Committee should modify its policy to one of greater ease.

December 3, 1963

1. Authority to effect transactions in System Account.

Information on economic and financial developments since the death of President Kennedy, while quite incomplete, suggested that the economy had shown little tendency to depart from the path of continued moderate advance in over-all activity and broad stability of commodity prices. Business and consumer confidence appeared to have remained firm and widespread. Unsettlement in sensitive commodity and security markets had been minimal, and corporate stock prices had quickly recovered from the losses suffered on November 22. Speculative switching out of dollars into other currencies or gold had been limited.

More complete data on domestic activity in October confirmed