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.

national payments, and seeking to avoid the emergence of inflationary pressures. This policy takes into account the continued orderly expansion in economic activity, relative stability in broad commodity price averages, and indications that the money supply is expanding rapidly again after some slackening in August and early September. It also gives consideration to current estimates that the deficit in the U.S. balance of payments in the third quarter continued at a high rate, although possibly not as high as in the preceding quarter.

To implement this policy, System open market operations shall be conducted with a view 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, Daane, Hickman, Mills, Mitchell, Robertson, Shepardson, Swan, Wayne, and Bryan. Votes against this action: None.

October 20, 1964

1. Authority to effect transactions in System Account.

Underlying domestic economic conditions apparently continued strong in recent weeks, although new uncertainties were introduced by recent political developments abroad and aggregate measures of domestic activity were being dampened by a work stoppage at a major automobile company, now in its fourth week. The industrial production index increased slightly in September despite a decline in automobile output. Weekly retail trade reports indicated little change in nondurable goods sales from the advanced August-September level, although durable goods volume declined in reflection of the shortage of new cars. Employment in nonfarm establishments rose further in September, but the unemployment rate, at 5.2 per cent, was little changed

from August. Wholesale industrial prices remained broadly stable into early October, except for further marked increases in nonferrous metals prices.

Gross national product was estimated to have advanced at an annual rate of $9 billion in the third quarter, to a level 6.9 per cent above a year earlier in current dollars and 4.8 per cent higher in real terms. Consumption expenditures rose more than disposable income in the quarter, and business outlays for fixed capital continued to expand vigorously. On the other hand, residential construction expenditures declined somewhat, and businesses accumulated inventories at an estimated annual rate of only $1.7 billion, $2 billion below the second quarter's moderate rate.

Total bank credit increased substantially again in September, with the rise concentrated in the first half of the month. Both loans and investments declined in early October. Growth in the money supply in September, and in the third quarter as a whole, was at an annual rate of about 6 per cent—twice the rate prevailing in the first half of the year. According to preliminary indications the money supply rose substantially further in the first half of October.

Free reserves of member banks continued to average about $80 million in the 3 weeks ending October 7. In the following week, however, they rose to an estimated $186 million, chiefly because the level of float over the Columbus Day holiday weekend was substantially higher than expected.

In security markets, yields on 3-month Treasury bills increased several basis points further to 3.59 per cent. Long-term markets were characterized by a cautious tone, and yields on long-term Treasury securities edged up after late September. Yields on new issues of corporate bonds declined in recent weeks as the calendar of forthcoming offerings contracted, but even in this market investor caution was suggested by a build-up in dealer inventories of unsold bonds. It was reported that the Treasury soon would announce the terms of its November refunding, which was expected to be a routine offering confined to the short-term area. At mid-October, prices of common stocks were at record levels.

Preliminary figures for the U.S. balance of payments in September showed a small over-all deficit for the month. The third-quarter deficit was estimated at an annual rate of about $2¼ billion, somewhat below the estimate for the preceding quarter. U.S. exports declined slightly in August, but the July-August trade surplus was little changed from the second quarter's $6 billion annual rate.

The Committee agreed that no change should be made in policy at this time in view of the forthcoming Treasury financing operation and of the uncertainties and unsettlements resulting from recent international political developments. In addition, some members thought a change in policy was not warranted at present either by domestic economic conditions or by balance of payments developments. Other members, however, believed that recent growth rates in bank credit and the money supply could not be sustained for long without increasing the inflationary dangers they thought already were incipient domestically. Serious concern also was expressed over the continuing sizable deficit in the U.S. balance of payments.

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 further expansion in economic activity, tempered by a work stoppage at a major automobile company; relative stability in broad commodity price averages, even though additional price increases have occurred in some materials markets; and indications that the vigorous money supply expansion of recent months continued in the first half of October. It also gives consideration to current estimates that the deficit in the U.S. balance of payments in the third quarter continued at a high rate, although not quite as high as in the preceding quarter.

To implement this policy, and taking into account the forthcoming Treasury financing, System open market operations shall be conducted with a view 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, Daane, Hickman, Mills, Mitchell, Robertson, Shepardson, Shuford, Swan, and Ellis. Votes against this action: None.

2. Authority to purchase and sell foreign currencies.

On several occasions since the spring of 1961 the Federal Reserve Bank of New York, acting for the account of the U.S. Treasury, had undertaken forward sales of selected foreign currencies for the purpose of reducing unduly high forward premiums on the foreign currency arising, for example, from market speculation based on expectations of a possible revaluation of that foreign currency. These operations had been successful in lessening pressures on the dollar and the U.S. gold stock.

At this meeting the Committee approved a recommendation of the Special Manager of the System Account that the Federal Reserve Bank of New York be authorized to conduct similar operations for System Account, within certain dollar limits, so that the System and the U.S. Treasury would be able to act in concert in the event a need for such operations should arise in the future. Specifically, it was agreed that the guidelines for foreign currency operations, as reaffirmed at the meeting of March 3, 1964, should be amended by deleting the second paragraph of Section 1 (cited below), and that the continuing authority directive for transactions in foreign currencies should be amended in two respects: to add a subparagraph (d) to the second paragraph authorizing forward transactions for the purpose indicated, and to revise the combined dollar limit for forward transactions for all authorized purposes from the figure of $150 million that currently applied to forward transactions for the three purposes already authorized to a figure of $200 million to cover the additional purpose for which forward transactions would be authorized as well.

At the same time, it was decided to make two further revisions in the continuing authority directive for foreign currency transactions. One revision consisted of the insertion of the word "concurrent" before the word "sales" in subparagraph (c) of the second paragraph, to clarify the distinction between the type of operation contemplated by this subparagraph and that contemplated by the new subparagraph (d). The other revision involved a change, from $2.05 billion to $2.1 billion, in the dollar limit specified in the first paragraph of the directive on the aggregate amount of foreign currencies held under reciprocal currency arrangements. It had been the Committee's practice to set this limit at the sum of the amounts currently specified by the Committee for all individual authorized reciprocal currency arrangements, which 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. This revision was made because earlier in the present meeting the Committee had approved an increase in the size of the reciprocal currency arrangement with the National Bank of Belgium from $50 million to $100 million.

In accordance with these decisions, the guidelines for System foreign currency operations were amended by deletion of the following paragraph from Section 1:

Holdings of a currency shall generally be kept sufficient to meet forward contracts in that currency (exclusive of contracts made under

parallel arrangements with foreign monetary authorities which provide their own cover) expected to mature in the following 3-week period.

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

Also in accordance with these decisions, the following continuing authority directive for transactions in foreign currencies was issued to the Federal Reserve Bank of New York:

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 3, 1964, as amended October 20, 1964; provided that the aggregate amount of foreign currencies held under reciprocal currency arrangements shall not exceed $2.1 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 $200 million 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;

(c) purchases through spot transactions and concurrent sales through forward transactions, for the purpose of restraining short-term outflows of funds induced by arbitrage considerations; and

(d) sales through forward transactions, for the purpose of influencing interest arbitrage flows of funds and of minimizing speculative disturbances.

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 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, Daane, Hickman, Mills, Mitchell, Robertson, Shepardson, Shuford, Swan, and Ellis. Votes against this action: None.

November 10, 1964

1. Authority to effect transactions in System Account.

Underlying domestic economic conditions appeared to have remained favorable in October despite work stoppages in the

automobile industry. Industrial production and retail sales apparently continued strong apart from the effects of interruptions in auto output, and over-all commodity price averages remained relatively stable. The unemployment rate was unchanged at 5.2 per cent.

Although declines in output in the auto and closely related industries were estimated to have reduced the index of industrial production for October by 2-3 percentage points, activity in other industries probably was maintained or increased further. New car sales were down sharply on a seasonally adjusted basis in October, but sales at furniture and appliance stores and at outlets for nondurable goods were up. Total construction activity edged down further in October, as residential building remained appreciably below the highs reached in the fall of 1963.

Strong upward pressures on wholesale prices were still limited to nonferrous metals. However, selective increases continued to be announced for other commodities, and recent weekly estimates showed a small increase in the average for industrial commodities. The consumer price index rose further in September at the slow pace of recent years.

Results of a private survey of business plant and equipment spending plans, taken in October, indicated that the level of such outlays planned for 1965 was about 5 per cent above the estimated 1964 total and little changed from the rate indicated for the final quarter of 1964 by the August Commerce–SEC survey. The increase in capital spending from 1963 to 1964 was estimated at about 14 per cent on the basis of returns in the private survey. While it was noted that actual outlays in years of business expansion often were larger than those reported as planned in the preceding autumn, these survey results still suggested some possible slowing from the recent growth rate in capital outlays.

Bank credit, after expanding sharply in September, was down moderately by the end of October according to preliminary estimates, perhaps partly because of the effects of the