FEDERAL RESERVE

press release

For immediate release May 20, 1974

The Board of Governors of the Federal Reserve System and the Federal Open Market Committee today released the attached record of policy actions taken by the Federal Open Market Committee at its meeting on February 20, 1974.

Such records are made available approximately 90 days after the date of each meeting of the Committee and are published in the Federal Reserve Bulletin and the Board's Annual Report. The summary descriptions of economic and financial conditions they contain are based on the information that was available to the Committee at the time of the meeting, rather than on data as they may have been revised since then.

Attachment

RECORD OF POLICY ACTIONS
OF THE FEDERAL OPEN MARKET COMMITTEE

Meeting held on February 20, 1974

Domestic policy directive

The information reviewed at this meeting suggested that real output of goods and services--which had grown at an annual rate of about 1.5 per cent in the fourth quarter of 1973--was declining in the first quarter of this year, mainly because of the oil situation, and that the GNP implicit deflator was continuing to rise rapidly. Staff projections suggested that weakness in economic activity would continue in the second quarter and that the rise in prices would remain rapid.

In January industrial production declined appreciably further, as output of automobiles and residential and commercial use of electricity and gas continued to decline while output of business equipment and other major categories of goods changed little; the January level was below the average in the fourth quarter of 1973. Nonfarm payroll employment fell sharply--reflecting sizable reductions in durable goods manufacturing and in contract construction--and the average workweek in manufacturing also declined considerably. The unemployment rate rose from 4.8 to 5.2 per cent. The dollar volume of retail sales recovered, following a sizable decline in December; although the January level was somewhat above the fourth-quarter average, the gain appeared to be less than the rise in prices of consumer goods.

Wholesale prices of industrial commodities continued to rise at a rapid pace in January; increases again were large for fuels and were substantial and widespread among other commodity groups. Wholesale prices of farm and food products also rose sharply, with increases especially large for prices of livestock, meats, and grains. In December the consumer price index had risen appreciably further, although the increase was tempered by declines in retail prices of meats and used cars. The index of average hourly earnings of production workers on nonfarm payrolls also had continued to advance in recent months, but at a less rapid pace than prices.

The latest staff projections for the first half of 1974 suggested that nominal GNP would expand somewhat less, and that real GNP would decline somewhat more, than had been anticipated at the time of the Committee's meeting in mid-January. Declines were concentrated in real consumption expenditures and residential construction activity, both of which were now projected to be weaker than had been expected 4 weeks earlier. As before, it was anticipated that the expansion in business fixed investment would remain relatively strong and that growth in State and local government purchases of goods and services would continue at a substantial rate. Business inventory investment was projected to be moderately below the high rate experienced in the fourth quarter of 1973, when stocks of large automobiles accumulated as sales fell off.

In foreign exchange markets the strong appreciation of the dollar that had begun in October gave way to depreciation near the end of January, reflecting in part the removal of U.S. controls on outflows of capital, relaxation of some foreign restraints on inflows of capital, and declines in U.S. interest rates relative to those abroad. In December U.S. merchandise exports had remained strong while imports had dropped from the very high level in November; the trade surplus had increased sharply both in December and in the fourth quarter as a whole.

Growth in total loans and investments at U.S. commercial banks accelerated in January, reflecting increases in most categories of loans and in banks' holdings of both Treasury and other securities. Expansion in business loans, which had been moderate in the fourth quarter of 1973, was especially strong in January, and business borrowing in the commercial paper market also was heavy. Between late January and mid-February, most banks lowered the prime rate applicable to large corporations from 9-3/4 to 9 per cent.

The narrowly defined money stock (M_1)[1/]--which had grown at a rapid pace in the last 2 months of 1973--declined in January; weekly data suggested that M_1 was expanding in early February. Inflows of consumer-type time and savings deposits increased substantially; as a result,

1/ Private demand deposits plus currency in circulation.

growth in the more broadly defined money stock (M_2)[2/] remained near the moderate rate in December. The outstanding volume of large-denomination CD's rose appreciably in January and, along with a large increase in U.S. Government deposits, contributed to an acceleration of growth in the bank credit proxy.[3/]

Net deposit inflows at savings and loan associations in January remained near the improved rate in the final months of 1973, but inflows to mutual savings banks fell off again. Growth in the measure of the money stock that includes such deposits (M_3)[4/]--like growth in M_2--continued near the moderate rate in December. Contract interest rates on conventional mortgages and yields in the secondary market for Federally insured mortgages declined between early January and early February.

On January 30 the Treasury announced that in early February it would auction up to $4.05 billion of notes and bonds to refund the bulk of $4.5 billion of publicly held notes and bonds maturing on February 15; the remainder would be retired by drawing down cash balances. In auctions on February 5, 6, and 7, respectively, the Treasury sold $1.50 billion of 7-year, 7 per cent notes at an average price to yield 6.95 per cent; $2.25 billion of 3-1/4-year, 6-7/8 per cent notes at an average price to yield

2/ M_1 plus commercial bank time and savings deposits other than large-denomination CD's.

3/ Daily-average member bank deposits, adjusted to include funds from nondeposit sources.

4/ M_2 plus time and savings deposits at mutual savings banks and at savings and loan associations.

6.70 per cent; and $300 million of 19-1/2-year, 7-1/2 per cent bonds at a price to yield 7.46 per cent to maturity.

System open market operations since the January 21-22 meeting had been guided by the Committee's decision to seek bank reserve and money market conditions consistent with moderate growth in monetary aggregates over the months ahead, while taking account of the Treasury's mid-February refunding and of international and domestic financial market developments. Soon after the meeting, incoming data suggested that in the January-February period the monetary aggregates would grow at rates well within the ranges of tolerance specified by the Committee; therefore, operations were directed toward a slight easing in bank reserve and money market conditions, in accordance with the Committee's instructions that such easing would be sought promptly if the data then available did not suggest that the aggregates were growing rapidly.

Around the beginning of February available data suggested that growth both in reserves available to support private nonbank deposits (RPD's) and in M_1 might fall below the specified ranges of tolerance. Therefore, the System sought some further easing in bank reserve and money market conditions. In the 2 weeks preceding this meeting the Federal funds rate was close to 9 per cent, compared with around 9-5/8 per cent in the days before the

January meeting; member bank borrowings averaged around $1,140 million in the 4 weeks ending February 13, little changed from the average in the preceding 5 weeks. Data that became available a few days before this meeting indicated that M_1 was expanding rapidly in early February and that it was likely to grow in the January-February period at a rate within the specified range; however, growth in RPD's still appeared likely to fall short of the specified range.

Short-term market interest rates had fallen appreciably since the Committee's meeting on January 21-22, in large part because money market conditions had eased, but also, apparently, because market participants expected them to ease further. On the day before this meeting the market rate on 3-month Treasury bills was 7.03 per cent, down from 7.97 per cent on the day before the January meeting.

Yields on longer-term securities also had declined somewhat, despite a large volume of financing in the capital markets and the sizable Treasury refunding. The over-all volume of new public offerings of corporate and State and local government bonds rose substantially in January, and an equally large volume was in prospect for February.

The Committee agreed that the economic situation and outlook continued to call for moderate growth in monetary aggregates over the longer run. Staff analysis suggested that, because of the lower projected rate of expansion in nominal GNP, the demand for money was likely to expand less over the first half of 1974 than had been expected earlier. In the February-March period, however, M_1 was expected to grow relatively rapidly, assuming little or no change in money market conditions; in February in particular, monetary expansion was expected to be spurred temporarily by an extremely sharp reduction in Treasury deposits. Relatively rapid M_1 growth over the February-March period appeared consistent with the Committee's longer-run objectives for the monetary aggregates because it would follow the sizable decrease of January and because it seemed likely to be temporary. In the event that money market conditions did remain about unchanged in the period immediately ahead, little or no further decline appeared likely in short-term market interest rates in general, and--to the extent that recent declines had been based on expectations of prompt further easing in money market conditions--rates could move up again.

Over the February-March period, according to the staff analysis, net inflows of consumer-type time and savings deposits to banks and nonbank thrift institutions were expected to remain sizable--with the effects of the recent declines in short-term market interest rates bolstered, perhaps, by increases in precautionary balances. Reflecting the availability of such funds, banks were not likely to issue substantial amounts of large-denomination CD's, even though business loan expansion might not moderate very much from the fast pace of January.

Taking account of the staff analysis, the Committee concluded that progress toward its longer-run objective of moderate monetary growth could be achieved with rates of expansion in the aggregates over the February-March period that were temporarily above those desired for the longer term. For the February-March period it adopted ranges of tolerance of 6-1/2 to 9-1/2 per cent and 9-1/2 to 12-1/2 per cent for the annual rates of growth in M_1 and M_2, respectively. The members agreed that rates of growth within those ranges would be likely to involve RPD growth during the February-March period at an annual rate within a 3-1/2 to 6-1/2 per cent range of tolerance, and they decided that in the period until the next meeting the weekly average Federal funds rate might be permitted to vary in an orderly fashion from as low as 8-1/4 per cent to as high as 9-1/2 per cent, if necessary, in the course of operations.

The members also agreed that, in the conduct of operations, account should be taken of international and domestic financial market developments. It was understood that the Chairman might call upon the Committee to consider the need for supplementary instructions before the next scheduled meeting if significant inconsistencies appeared to be developing among the Committee's various objectives and constraints.

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

The information reviewed at this meeting suggests that real output of goods and services is declining in the current quarter, mainly because of the oil situation, and that prices are continuing to rise rapidly. In January industrial production declined again, nonfarm payroll employment dropped, and the unemployment rate rose above 5 per cent. Prices of both farm products and industrial commodities increased very sharply. Wage rates have continued to rise substantially in recent months, although not so sharply as prices.

After having appreciated for several months, the dollar has declined somewhat on the average against foreign currencies in recent weeks. U.S. controls on capital outflows were removed at the end of January, and several foreign countries have relaxed controls on capital inflows. The U.S. trade surplus rose sharply in December and in the fourth quarter as a whole.

The narrowly defined money stock, after increasing substantially in the last 2 months of 1973, declined in January; most recently, however, it has appeared to strengthen. Broader measures of the money stock continued to rise in January, as net inflows of consumer-type time deposits remained relatively strong. Expansion in business loans and in total bank credit accelerated, and banks stepped up issuance of large-denomination CD's. Since mid-January, short-term market interest rates have fallen appreciably, and long-term rates have declined somewhat.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster financial conditions conducive to resisting inflationary pressures, cushioning declines in production and employment that are being induced in large part by the oil situation, and maintaining equilibrium in the country's balance of payments.

To implement this policy, while taking account of international and domestic financial market developments, the Committee seeks to achieve bank reserve and money market conditions consistent with moderate growth in monetary aggregates over the months ahead.

Votes for this action: Messrs. Burns, Hayes, Balles, Brimmer, Daane, Holland, Mayo, and Mitchell. Votes against this action: Messrs. Bucher, Francis, Morris, and Sheehan.

The members dissenting from this action did so for different reasons. Messrs. Bucher, Morris, and Sheehan expressed concern about current and prospective weakness in aggregate economic demands. In order to encourage further declines in short- and long-term interest rates, including mortgage rates, they favored somewhat higher ranges of tolerance for the monetary aggregates and a lower range for the Federal funds rate than the Committee had agreed would be consistent with the directive. Mr. Francis expressed the view that the over-all economic situation was stronger than suggested by the staff projections and that inflation remained the major long-term economic problem. He dissented because he thought the policy adopted by the Committee would permit the money stock to grow at a faster rate than was consistent with progress in dealing with inflation.

Subsequent to the meeting it appeared that in the February-March period growth in the monetary aggregates would equal or exceed the upper limits of the short-run ranges of tolerance specified by the Committee. In view of that behavior, the System ordinarily would have become more restrictive in its reserve-supplying operations, expecting that the weekly-average Federal funds rate would rise toward the upper limit of its range of tolerance--namely, 9-1/2 per cent. On March 1, however, a majority of the available members[5/] concurred in a recommendation by the Chairman that in light of the recent marked rise in market interest rates and the highly sensitive state of financial markets, the System conduct reserve operations in a manner expected to be consistent with maintenance of the funds rate at the prevailing level of about 9 per cent, for the time being.

One week later, it appeared that strong growth in the monetary aggregates was persisting. On March 11, in view of that behavior, the available members--with the exceptions of Messrs. Bucher and Sheehan--concurred in a recommendation by the Chairman that the System return to conducting reserve operations in a manner consistent with the full range of tolerance for the Federal funds rate agreed upon at the February meeting. However, in light of recent increases in market interest rates and the sensitive state of financial markets, the Account Manager would be expected to proceed very cautiously in operations thought likely to be consistent with a rise in the weekly average funds rate above 9 per cent.

5/ The members and alternate members of the Committee newly elected by the Federal Reserve Banks took office on March 1 for the term of one year commencing on that date. Mr. Coldwell, responding as alternate for Mr. Kimbrel, did not concur in the Chairman's recommendation.

FEDERAL RESERVE

press release

For Immediate Release May 17, 1974

The Board of Governors of the Federal Reserve System today announced the appointment of Mr. Charles R. McNeill as an Assistant to the General Counsel. Mr. McNeill's primary responsibilities will be in the areas of legislative analysis and bank holding company matters.

Mr. McNeill holds a B.A. degree from Amherst College and a J. D. degree from the Harvard Law School. He joined the Treasury Department's legal staff in 1943 where he worked on the administration of gold and silver regulations. Between 1946 and 1952, he worked at the Treasury on legal matters relating to exchange rates, trade, payments problems and foreign lending. During this period, he also acted as Counsel to the Staff Committee of the National Advisory Council on International Monetary and Financial Policies. In 1952, he was named Assistant General Counsel at Treasury. He resigned his Treasury post in 1956 to accept a position as Assistant General Counsel of the American Bankers Association. In 1962, he was appointed Director of ABA's Washington office.

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FEDERAL RESERVE
press release

For Immediate Release May 20, 1974

The Board of Governors of the Federal Reserve System today announced two regulatory changes designed to aid the development of banks in low income or other economically depressed areas.

One of the regulatory amendments makes an exception under Regulation L to permit interlocking personnel relationships, under certain conditions, in low income or depressed areas. Generally, directors, officers and employees of member banks are prohibited from holding similar positions in another bank, savings institution or trust company in the same, or adjacent, communities.

The second makes an exception under Regulation Y to permit a bank holding company which provides bank management consulting advice to an unaffiliated bank in a depressed or low income area, to have interlocking personnel relationships with the nonaffiliated bank. In general, Regulation Y does not permit a bank holding company to give management consulting advice to a non-affiliated bank if there are interlocking personnel relationships.

The amendments are to be effective June 20, 1974.

Interlocking personnel will be permitted only upon the following conditions:

-- Any director, officer or employee of a member bank may be a director, officer or employee of not more than one other bank, located or to be located, in a low income or economically depressed area;

-- The interlocking relationship is necessary to provide management or operating expertise;

-- There are no more than three interlocking relationships between any two banks, and interlocking personnel do not constitute a majority of the board of directors of the bank being assisted;

-- Interlocking relationships are not to last more than five years; and

-- The Board may determine other terms and conditions in specific cases in addition to, or in lieu of, the above.

The Board also adopted an interpretation of its amendment to Regulation L setting forth criteria that may be used in designating a "low income or other economically depressed area". The Board said such an area is one, without regard to political or other subdivisions or boundaries, that has some or all of the following characteristics:

-- A rate of unemployment substantially above the national average.

-- A median level of family income significantly below the national median.

-- The economy of the area has traditionally been dominated by one or two industries and these are in a state of long-term decline.

-- Labor and capital are leaving the area to a substantial degree.

-- The area is adversely affected by changing industrial technology.

-- The area is adversely affected by changes in national defense production or facilities.

Copies of the Board's orders are attached.

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TITLE 12--BANKS AND BANKING

CHAPTER II--FEDERAL RESERVE SYSTEM

SUBCHAPTER A--BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

[Reg. L]

Part 212--Interlocking Bank Relationships
Under the Clayton Act

By notice of proposed rulemaking, published in the Federal Register on February 19, 1974 (39 Federal Register 6132), the Board of Governors proposed to permit under certain circumstances interlocking service by a director, officer or employee of a member bank with another bank, banking association, savings bank or trust company located in a low income or other economically depressed area, by amending § 212.3 of the Board's Regulation L.

Following consideration of the comments received, the Board has amended § 212.3, effective June 20, 1974, to permit certain interlocking relationships with minor modifications in language from that originally proposed.

An accompanying interpretation sets forth illustrative criteria that may be used in determining whether a certain area is a "low income or other economically depressed area."

The text of the amendment to § 212.3 reads as follows:

§ 212.3 Relationships permitted by Board.

In addition to any relationships covered by the foregoing exception, not more than one of the following relationships is hereby permitted by the Board of Governors of the Federal Reserve System in the case of any one individual.

* * * * *

(g) Bank in low income area. Any director, officer or employee of a member bank of the Federal Reserve System may be at the same time a director, officer or employee of not more than one other bank located, or to be located, in a low income or other economically depressed area, subject to the following conditions: (1) such relationship is determined by the Board to be necessary to provide management or operating expertise to such other bank; (2) not more than three interlocking relationships between any two banks shall be permitted by this paragraph, except that persons serving in interlocking relationships pursuant to this paragraph shall in no instance constitute a majority of the board of directors of the other bank; (3) no interlocking relationship permitted by this paragraph shall continue for more than a five-year period, and (4) upon such other terms and conditions in addition to or in lieu of the foregoing, as may be determined by the Board in any specific case.

* * * * *

The Board has also adopted an interpretation relating to certain terms used in the regulation as set forth below.

§ 212.103 Exemption from section 8 of the Clayton Act for Banks in low income areas.

(a) Effective June 20, 1974, the Board of Governors amended section 212.3 of Regulation L to exempt under certain circumstances from the prohibitions of section 8 of the Clayton Act (15 U.S.C. § 19) interlocking relationships between a member bank and a bank in a "low income or other economically depressed area". (12 CFR 212.3(g)). This interpretation is intended to set forth some of the criteria that may be used in the designation of such an area.

(b) A "low income or other economically depressed area" is any area, without regard to political or other subdivisions or boundaries, which have some or all of the following characteristics:

(1) the rate of unemployment is substantially above the national rate;

(2) the median level of family income is significantly below the national median;

(3) the economy of the area has traditionally been dominated by only one or two industries, which are in a state of long-term decline;

(4) the rate of outmigration of labor or capital is substantial;

(5) the area is adversely affected by changing industrial technology;

(6) the area is adversely affected by changes in national defense facilities or production.

By order of the Board of Governors of the Federal Reserve System, May 17, 1974.

(Signed) Theodore E. Allison

Theodore E. Allison
Assistant Secretary of the Board

[SEAL]

TITLE 12--BANKS AND BANKING

CHAPTER II--FEDERAL RESERVE SYSTEM

SUBCHAPTER A--BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

[Reg. Y]

PART 225--BANK HOLDING COMPANIES

Bank Management Consulting Advice

Section 225.4(a)(12) of Regulation Y permits bank holding companies to offer management consulting advice to nonaffiliated banks subject to certain conditions. One of those conditions is that there be no interlocking personnel relationships between the bank holding company or any of its subsidiaries and the unaffiliated bank.

By action effective June 20, 1974, the Board has amended section 212.3 of the Board's Regulation L ("Interlocking Relationships under the Clayton Act" (12 CFR 212)) so as to permit interlocking personnel relationships between a member bank and a bank located in a low income or other economically depressed area. The public interest which the amendment to Regulation L serves would similarly be served by a relaxation of the restriction found in § 225.4(a)(12)(ii). Thus, the purpose of the present amendment is to permit a bank holding company to extend management consulting advice to an unaffiliated bank with which the bank holding company or any of its subsidiaries has established interlocking relationships pursuant to section 212.3(g) of Regulation L.

The text of the amendment to § 225.4(a)(12)(ii) reads as follows:

§ 225.4 Nonbanking Activities

(a) Activities closely related to banking or managing or controlling banks * * *. The following activities have been determined by the Board to be so closely related to banking or managing or controlling banks as to be a proper incident thereto.

*   *   *   *   *

(12) providing management consulting advice* to nonaffiliated banks Provided that, * * * (ii) no officer, director or employee of the bank holding company or any of its subsidiaries serves as an officer, director or employee of the client bank, except where such interlocking relationships are or would be permitted by section 212.3(g) of Regulation L; * * *

The notice and public participation procedure described in section 553 of Title 5, United States Code in unnecessary in connection with this amendment for the reasons and good cause found by the Board, because this amendment operates to relieve restrictions otherwise

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*In performing this activity bank holding companies are not authorized to perform tasks or operations or provide services to client banks either on a daily or continuing basis, except as shall be necessary to instruct the client bank on how to perform such services for itself. See also the Board's interpretation of bank management consulting advice (12 CFR 225.130).

applicable under § 225.4(a)(12) of Regulation Y, and such procedure would not aid the persons affected or otherwise serve any useful purpose.

Effective date: June 20, 1974.

By order of the Board of Governors of the Federal Reserve System, May 17, 1974.

(Signed) Theodore E. Allison

Theodore E. Allison
Assistant Secretary of the Board

[SEAL]

FEDERAL RESERVE

press release

For Immediate Release May 13, 1974

The Board of Governors of the Federal Reserve System announced today the appointment of Paul Wonnacott, Professor of Economics at the University of Maryland, as an Associate Director in the Division of International Finance.

Mr. Wonnacott holds a B. A. degree from the University of Western Ontario and Master and Doctorate degrees from Princeton University. He was a Fellow at The Brookings Institution in Washington in 1957-58 and was an instructor and assistant professor of economics at Columbia University from 1958 to 1962. He served on the research staff of the Canadian Royal Commission on Banking and Finance in 1962 and later that year became an associate professor of economics at the University of Maryland. Mr. Wonnacott was a Ford Foundation Fellow in 1963-64 and was senior staff economist for the Council of Economic Advisers, 1968-70.

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With the Compliments
of

RICHARD A. DEBS
First Vice President

FEDERAL RESERVE BANK OF NEW YORK

No acknowledgment necessary.

Remarks by

Richard A. Debs
First Vice President
Federal Reserve Bank of New York

before the

Government Development Bank for Puerto Rico

on

February 22, 1974

INFLATION, ENERGY AND THE ECONOMIC OUTLOOK

INFLATION, ENERGY AND THE ECONOMIC OUTLOOK

This morning I would like to spend some time with you reviewing the current economic situation and the outlook for the coming year. As you know, it is a subject that has been receiving a good deal of attention these days. The best way to start, of course, is to look at some of the significant developments of the past year and their implications for the new year.

1973 was quite a year for the economy. It will be remembered for many things. It started out with the termination of the Phase III controls in January, quickly followed by an international currency crisis and the second devaluation of the dollar in February. And the year ended in December with the economy--and the world in general--still dazed by the effects of the oil embargo, but finally attempting to come to grips with the underlying problem of energy shortages. It was also a year that saw the Dow Jones average slide by over 150 points between January and December.

Looking back at the year as a whole, however, perhaps its most important characteristic--and one whose importance was not as well recognized as it might have been--is that 1973 was a boom year, a year of exploding prices, a year of burgeoning inflation, and a year marked by enormous pressures on productive facilities.

As you can see (Chart 1: Real GNP), real output rose extraordinarily over much of 1972 and through the first quarter of 1973, measured in terms of both real GNP and industrial production. As a result, the economy suffered severe capacity constraints beginning early last year--a development that many economists, statisticians, and policymakers were slow to recognize. The conventional view in late 1972 was that, because the overall unemployment rate remained significantly over 4%, output limits were still quite distant. In retrospect, this was a misjudgment, and in some respects it may have encouraged overly expansive monetary and fiscal policies in 1972. By early 1973, the serious pressures we still see today had already been developing.

These pressures show clearly in the economic barometers. Capacity utilization of major materials-producing industries was at record levels (Chart 2: Capacity Utilization Index). This factor--the nearly complete utilization of capacity--and not tightness in the labor markets--was the most conspicuous bottleneck in the economy during the year.

Labor markets were, of course, fairly tight during most of 1973, with the unemployment rate (Chart 3: Unemployment Rates) dropping to 4.6 percent in October. That figure may not seem to indicate substantial tightness compared with historical figures--such as the low of about 3.5 percent in the late 1960s. However, the overall rate doesn't provide the best historical measure because of the rising proportion of young people and women in the labor force, two groups with above average unemployment rates. In any case, while the labor markets were relatively tight last year, they have been as tight or tighter before, and they do not seem to have been the primary cause of supply constraints during the year.

In retrospect, it seems clear that it was primarily the strain on capacity, which was world-wide, compounded by a number of other factors (such as grain and protein shortfall), that resulted in a rather distressing price performance for the year--and despite the continued existence of a price control program under Phase III (Chart 4: Consumer Prices). The situation was aggravated by the additional pressure that resulted from the abrupt spurting of prices as soon as Phase II was terminated, the devaluation of the dollar, the subsequent reemergence of excess demand, and the further rounds of price increases in anticipation of the reimposition of stricter controls.

As you will recall, the price explosion that took place at the beginning of Phase III subsequently led to the two-month price freeze starting June 13, and then the establishment of the Phase IV controls in mid-August. Phase IV is still with us; and although it may be too soon to pass final judgment, no one can be very enthusiastic about it. Since June, consumer price increases have actually accelerated, even compared to Phase III. In any case, the Administration is willing to allow statutory authority for controls to lapse at the end of April, except for fuel and health care.

Consumer prices haven't yet fully reflected the advances in wholesale industrial prices (Chart 5: Industrial Prices.) We don't know what the ultimate effects will be, but in any case, we can't be too optimistic about the future.

Looking back, with the benefit of hindsight, at the overall control program, while Phase II looked successful, it is now clear to most observers that subsequent developments had distorting, disincentive effects in many cases, encouraging exports and discouraging domestic production precisely in those areas where shortages have been worst. Perhaps just as important is the fact that this performance has generated a widespread disillusionment with controls on the part of both business and labor.

Some cautious optimism on the price outlook for 1974 developed last fall as food prices dropped well off their August peaks (Chart 6: Spot Food Prices). It didn't seem likely the 1973 price bulge would be repeated, since world demand pressures on commodity prices generally appeared to be abating. In addition, the worst of the post-freeze bunching of industrial price increases seemed likely to be completed early in 1974. But the energy shortage has darkened that prospect, and now fuel prices are playing the earlier role of food prices as the chief villian in the inflation drama.

Nobody seems to be too sanguine about the prospects for prices in 1974. The range of the most recent published forecasts for 1974 prices (Chart 7: Deflator Forecasts) is rather wide, reflecting deep uncertainties, but they all indicate continuing high levels of inflation. (Incidentally, the deflator figure shown on the chart is well below the rate of growth of the consumer price index, which rose at an 8.8 percent rate between December 1972 and December 1973.) The Council of Economic Advisers had forecast a 7 percent increase in the GNP price deflator. Even the low end of the range is a relatively high 5 percent, and even that is wishful thinking--although it's not impossible that improvement by the second half might materialize.

Turning to forecasts of gross national product, current statistics show a definite slowing in the economy that, so far, seem consistent with the consensus forecast of a slowdown in real GNP. However, it is impossible to be sure how far the trend will carry.

Growth in industrial production and real output slowed sharply in the fourth quarter. As we saw in Chart 1, industrial production actually declined in December and January largely as a result of energy cutbacks and slowing production in the auto industry, which has its special, and partly energy-related problems.

It seems clear that production will continue to be damped by energy shortages and the auto industry's problems during the early months of this year. For example, in January (Chart 8: Autos) new car output was at its lowest rate since the 1970 GM strike, and February production schedules indicate even deeper cuts.

The unemployment figures are also reflecting some slowing in the economy, partly because of the energy situation. The rate rose from a low of 4.6 percent in October to 5.2 percent in January. At this point, it would appear that, with the present labor market structure and composition, unemployment rates of under 5 percent can't be sustained for too long without accelerating inflation rates. Nevertheless, unemployment rates could well rise this year--at least for a time--to clearly undesirable levels.

Turning to the outlook for demand, we see areas of both weakness and strength. Housing is the primary example of weakness (Chart 9: Private Residential Construction).

The recent levels of housing starts have been low in relation to the longer-run growth trend. If savings continue to flow into thrift institutions, most analysts assume that an upturn will develop by mid-year.

The second most obvious area of demand weakness is cars. Of course, an easing of the gas shortage and the completion of plans to shift output to smaller cars would eventually provide a lift. However, it should also be noted that after adjusting for price increases, retail sales excluding autos (Chart 10: Retail Sales Excluding Automotive) have been essentially flat for many months.

On the optimistic side, one area of seemingly clear prospective strength is business capital spending (Chart 11: Plant and Equipment). Various government and private surveys suggest a 12-14 percent rise in business capital spending this year, which isn't surprising given the capacity problems in many industries.

Another plus in the outlook is the low level of inventories relative to sales--with the conspicuous exception of standard-size cars. (Chart 12: Inventories). Indeed, shortages are probably holding stocks below desired levels in some fields. Thus, on balance, there are no signs of impending excess-inventory problems that have been associated with most postwar recessions.

As far as the Federal budget is concerned, the projected fiscal 1975 deficit (Chart 13: Federal Budget) is scheduled to rise moderately, mainly because a slower economy should cut tax receipts (Chart 14: Rise in Receipts). However, it seems more pertinent that there is likely to be another large rise in outlays (Chart 15: Rise in Outlays). On balance, we would characterize the 1975 budget as being like the current fiscal 1974 budget--moderately stimulative.

As for monetary policy, in retrospect it is now generally agreed that the growth of monetary aggregates in 1972 was somewhat excessive (Chart 16: M_1 and Bank Credit). The Federal Open Market Committee wasn't willing at that time to see money market conditions tighten up to the degree and with the speed necessary to ensure a slower growth rate. In 1973, however, a number of steps were taken to lower the growth of these aggregates to a more moderate rate. For example, marginal reserve requirements on large CDs and related bank sources of funds were raised. The discount rate (Chart 17: Selected Money Market Indicators) was raised in six steps to the current all-time peak of 7.5 percent. Most important, open market operations were aimed at bringing the monetary aggregates under tighter control.

While everyone would agree that we went through a period of relatively tight money in 1973, there are various ways of assessing just how tight it was. M_1 (checking account balances and currency outside banks) averaged a moderate and appropriate 5.7 percent over 1973 as a whole. Within the year, however, the aggregates showed, as always, wide short-run fluctuations (Chart 18: $\underline{M_1}$).

This may be a good point to note that the Federal Reserve's ability to control the growth rates of the money supply and bank credit over short periods is very limited. Moreover, short-run deviations--say, up to six months--from longer-term objectives are probably not damaging to the economy, at least if they are subsequently offset. I'm afraid that there is a widespread tendency to try to over-interpret these short-run movements. As you can see, they are rather erratic on a monthly basis.

As for bank credit growth, it was quite rapid, partly because of the assignment of the Committee on Interest and Dividends, under the control program, to hold bank loan rates from rising as fast or as far as they might otherwise have. As a result, banks were an unusually cheap source of funds until open market rates, such as the commercial paper rate, began falling in September (Chart 19: Selected Interest Rates). Thus, more lending moved through the banking system earlier in the year than would have been normal for a tight-money period. Banks financed the loan expansion by issuing CDs, a technique that was enhanced by the absence of Regulation Q ceiling restraints. Since the fall, open market rates have fallen from their peaks, rate relationships have been restored more nearly to normal, and bank loan growth has slowed markedly.

Slowing the money supply growth rate in the face of a strongly advancing economy involved some very sharp short-term rate advances to historical peaks by late summer (Chart 20: Selected Money Rates). Indeed, the behavior of short rates is the only measure by which money could be characterized as being exceptionally tight in 1973. The slowing in the growth of the monetary aggregates was less pronounced than in several other periods of restraint. Moreover, there was very little indication of credit rationing and credit shortages this time--with the exception of housing after June. Although monetary policy in particular, and financial conditions in general, helped encourage some needed slowing in the economy, they at no time produced conditions of extreme restraint.

As for GNP forecasts for 1974, you will recall that last fall, a consensus was emerging that the economy's growth would be noticeably less rapid in 1974, but that we would avoid a recession. An October survey of private forecasts showed a median year-to-year rise in real GNP of about 2.5 percent. (Chart 21: Real GNP). This would have been significantly below the "normal" growth trend--usually reckoned at 4 to 4.5 percent--and would have been compatible with very small or near zero growth in some individual quarters in 1974.

But then came the Arab oil embargo, and the fall forecasts--which looked quite reasonable at the time--had to be reconsidered. The old forecast is still useful, however, as a base line from which to measure the possible economic implications of the oil embargo. It appears that, on average, forecasters have cut their estimates of real GNP growth this year by about 1 percentage point. This is a significant, but still moderate, reduction. One survey, taken in December, suggests that most economists were then estimating real growth for 1974 at between zero and 2.5 percent, with many estimates clustering around a median of 1.5 percent. These forecasts generally assume, incidentally, that the oil embargo will be over by mid-year. The Council of Economic Advisers is estimating about 1 percent real growth for 1974. Thus, the official government forecast is actually a shade more pessimistic than the December consensus.

If growth turns out to be around 1 to 1.5 percent for the year, one or two quarters of outright declines in output would be a reasonable expectation. Also implicit in such a forecast is some rise in the unemployment rate, perhaps to the 5.5 to 6.0 percent range.

The economic outlook, which is always uncertain, is of course open to an especially high degree of uncertainty this year. First, there is obviously a very real question of how long the Arab oil restrictions will remain in effect. Second and equally obvious, is a question of just how effective the restrictions are turning out to be, and how serious a shortage will actually develop. Until

January, imports were running above expectations (Chart 22: Petroleum Imports), suggesting leaks in the embargo. Inventories seem to be still higher than might have been expected (Chart 23: Petroleum Inventories).

As a result of these developments, the Government has twice pared its estimate of the first-quarter shortfall between normal consumption demands and available supplies. The original estimate of 3.5 million barrels per day has been trimmed to the present 2.7 million. The actual shortfall, however, could be lower. Of course, we still don't know what impact all this will have on the economy. It is still only February, and most of our latest economic data refer to December or early January, when the effects of the boycott were just beginning to be felt.

To sum up, the current picture of the economy is a mixture of clear pluses, clear minuses and clear question marks: There are still many signs of shortages and demand pressures, together with some definite indications of ebbing demand in other areas. On balance, I would think that we are seeing about what might be expected in terms of the standard forecast--in other words, a relatively brief, relatively mild, and partly shortage-induced downturn. While this will produce problems, it should at least create some breathing space in the economy, something which is absolutely necessary if our really dangerous rate of inflation is to be tamed. However, the art of forecasting being what it is, it would be both futile and dangerous to think that we can achieve any certainty about the possible extent of the economic slowdown. Clearly, we have to watch developments, particularly for any signs of a cumulative weakening of demand.

One might question the role of monetary policy in our present situation, where we have rampant inflation coupled with a slowing in the economy that has been aggrevated by a fuel shortage. Let us touch briefly on a few of the possibilities.

First, if the oil embargo ends soon, the worse effects of the immediate oil shortage should dissipate in a few months, although the effects of substantially higher oil prices will no doubt be with us for a long time. Given several months' lag in the impact of monetary policy on real activity, and the even longer lag in its effect on prices, there is a serious question as to whether monetary policy could or should do much to attempt to deal with the effects of the embargo itself.

If, on the other hand, the oil shortage appears likely to be both deep and protracted, there are some conflicting considerations. Inflation will worsen, and that by itself might seem to suggest a less accommodative monetary policy. Moreover, to the extent that production cutbacks represent supply limitations alone, increased credit and money could do nothing--except, perversely, to provide additional funds to bid prices higher on the reduced supply of goods. In a word, the central bank can issue dollars, but it can't pump oil.

This isn't the whole story, however. As the supply constraints cut into production, then income and profits--and therefore demand--could fall by more than just the original supply effects of the shortage. The result could conceivably be a weakening in the economy well beyond what is desirable to relieve excess demand pressures. In that case, it is not impossible that some offsetting stimulus from monetary policy would be in order.

Looking beyond our immediate problems, the economy, no doubt, will have to adjust to a long-run decline in the availability of cheap energy, but this isn't primarily a problem for monetary policy. In my opinion, monetary policy's central concern is to break the inflationary spiral we have been caught in over the last several years.

Looking for a moment to the international side, we start 1974 with a wide range of possibilities. There was a substantial improvement in the U.S. trade position over the course of 1973, with a year-to-year turn-around of about $8 billion in our net exports. (Chart 24: Exports and Imports). As you can see, our agricultural exports moved up very sharply. Non-agricultural exports, including a very wide range of goods, also showed substantial gains. (Chart 25: U.S. Exports). It seems clear that in many areas our goods are once again competitive. (Chart 26: Comparative Export Prices). Indeed, exports certainly would have been higher if we had had the capacity necessary to produce more.

On the import side, (Chart 27: Imports) the dollar cost rose significantly further but, excluding fuels, the real volume of imports, in constant dollars, on balance actually declined over the year. The decline reflected the significant change in costs resulting from the dollar devaluations, as well as the fact that foreign productive capacity abroad was stretched tight by world-wide boom conditions.

There are a couple of things that emerge from these trade charts that may be useful in helping us look ahead. On agricultural goods, one chart showed the volume of exports holding relatively steady following the initial jump in the first quarter, while most of the rest of the gain resulted from price increases. The general expectation seems to be that our agricultural exports will remain strong. However, we shouldn't be surprised to see some attrition if harvests improve abroad, in which case price pressures here should be relieved.

With respect to other goods, it is clear that we are again in a relatively strong competitive position in the non-agricultural area. As the economy slows and capacity limitations are less of a constraint, we should be able to continue to increase our share of nonagricultural exports. The major uncertainty in the outlook for this area is the level of economic activity abroad, particularly in relation to the impact of oil-related problems on industry, and the efforts that foreign countries may make to finance increased oil bills with expanding exports.

There is little reason to expect a deterioration in our import position apart from fuels, since the economy is likely to slow. Imports of smaller foreign cars may rise, but we shouldn't expect that to be a significant problem in the overall picture. Fuels, of course, are another story. All that can be said with any certainty is that the nation's oil bill will grow substantially. It is easy to project an increase of $9-10 billion in 1974, based on September 1973 imports and January 1, 1974 prices. But both of these assumptions are clearly open to question. In view of the magnitude of the uncertainties, it is very difficult to guess how the overall balance of trade will come out at the end of 1974.

Looking for a moment at the question of capital flows, it seems clear that the reopening of the U.S. market for long-term borrowing will lead to some outflow on that account, with recent estimates running from $1.5 to $2 billion, all the way to $4 billion. However, we could well see a further rise in long-term capital inflows similar to the kind that began emerging in 1973. Moreover, it is likely that some portion of the excess receipts of the oil producers will turn up in the United States directly or indirectly in medium to long-term forms.

Short-term capital flows are obviously going to be subject to a variety of conflicting forces. There may be some shifting of short-term lending abroad from overseas branches to head offices of U.S. banks. However, the short-term flows will probably be highly interest-rate sensitive and will depend greatly on relative interest rates in the United States and in Europe These in turn may be greatly affected by how other countries finance their oil deficits and where the Arabs put their short-term deposits. It is impossible to say which way the net flow will go at this point, but it seems likely that short-term rates here and abroad will tend to converge more than in recent years.

Finally, we should spend a few moments on the exchange rate situation. (Chart 28: Dollar Exchange Rates). As you are aware, the efforts of the past two years to achieve a comprehensive and formal monetary reform have not been especially fruitful, particularly in the light of recent developments. It has been clear for quite a while that there has been only limited agreement achieved, and even then only in broad terms, with considerable disagreement over crucial operational details. Meanwhile, during the past year we have had a regime of "managed" floating--"managed" primarily by means of central bank intervention. If we add up official intervention in the exchange markets since floats began in March 1973, the total is near $30 billion, a figure probably exceeding the intervention over any similar period under fixed rates. Despite this massive amount, we have continued to have very substantial and often erratic movements in exchange rates. Considering the events of the past year, both economic and noneconomic, it is doubtful that we could have done better under any other system. However, I don't think that our experience makes a very persuasive case for floating rates.

Gabriel Hauge of Manufacturers Hanover Trust Company in New York City put it very well recently when he said:

> "Although most economists still appear to favor a floating exchange rate system, careful monitoring of the current experiment in floating has not been reassuring, at least to me. At times last year, the major currencies fluctuated sharply against each other, leading to the kind of highly unstable situation that floating was suppose to obviate. The system made it possible for the dollar to be driven down to an unreasonable level against many other currencies, so that the U.S. public is now paying the price in terms of added inflation for the instability of the floating rate system. As I contemplate the recent experience with the theoretically appealing case for floating, I cannot but recall Charles Kettering's warning, 'Beware of logic; it is an organized way of going wrong with confidence.'"

In the end it seems rather clear that the only factor that has helped to carry the monetary system through the shocks of the past six months has been the growing strength of the dollar. Regardless of how much people want a substitute, and how much they want to reduce the system's dependence on the dollar, that dependence inevitably will continue for some time. Consequently, restoration and maintenance of confidence in the dollar still remain the keys to reasonable stability in the monetary system. As Chairman Burns stated recently to the Congress:

> "...Confidence in the dollar is essential both to a healthy domestic economy and to a successful evolution of the international monetary system. Looking to the future, we must strive to conduct all our economic policies--domestic as well as international--in such a manner that they will maintain, and indeed strengthen, that confidence."

Confidence is indeed essential. And confidence cannot be won unless and until it can be clearly demonstrated that the forces of inflation--which have been with us for so long--can and will be brought under control. Hopefully the coming year will see a substantial movement toward that goal.

CHARTS

presented at

Government Development Bank for Puerto Rico

February 22, 1974

Richard A. Debs

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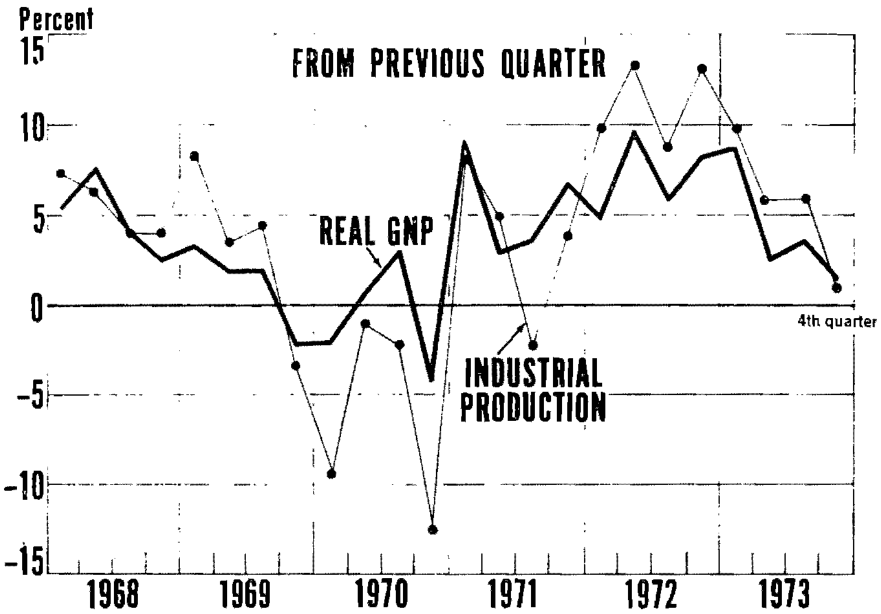

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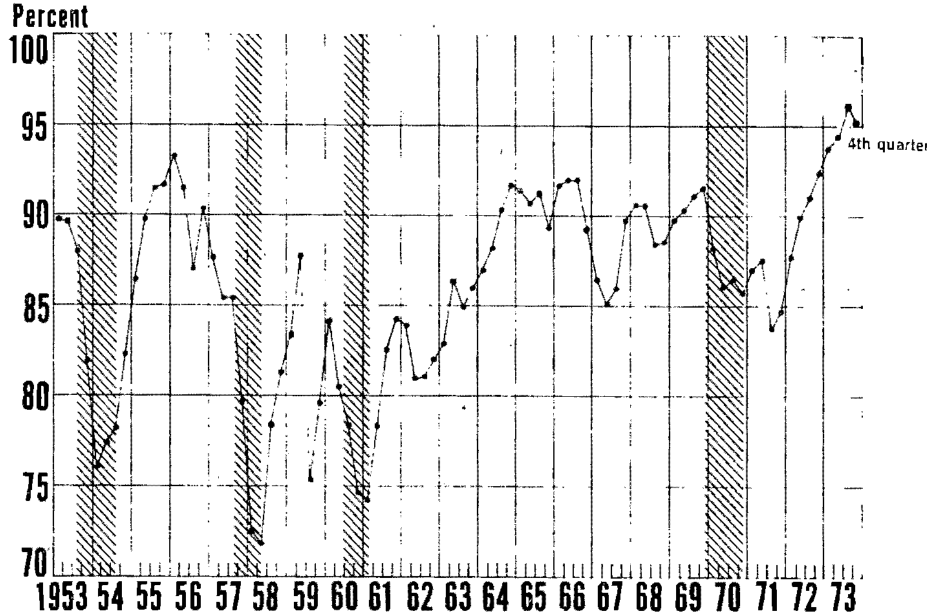

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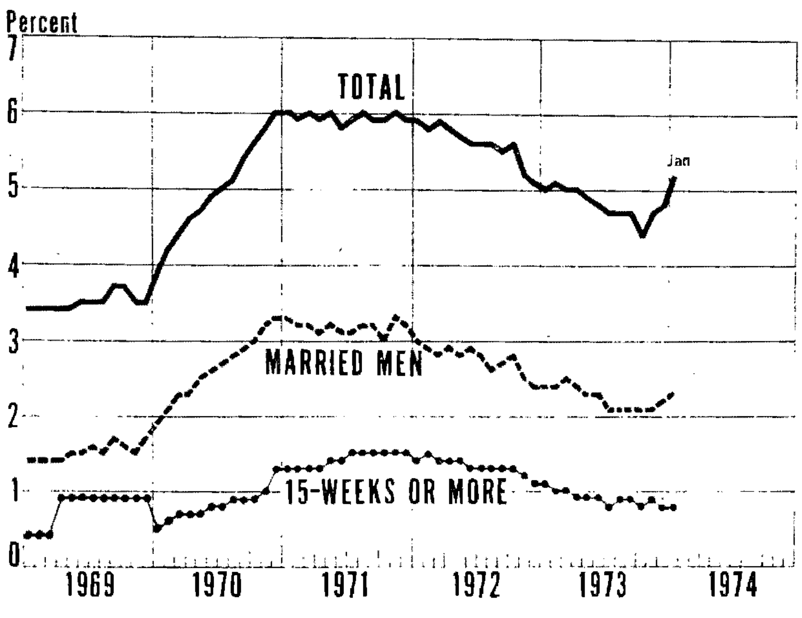

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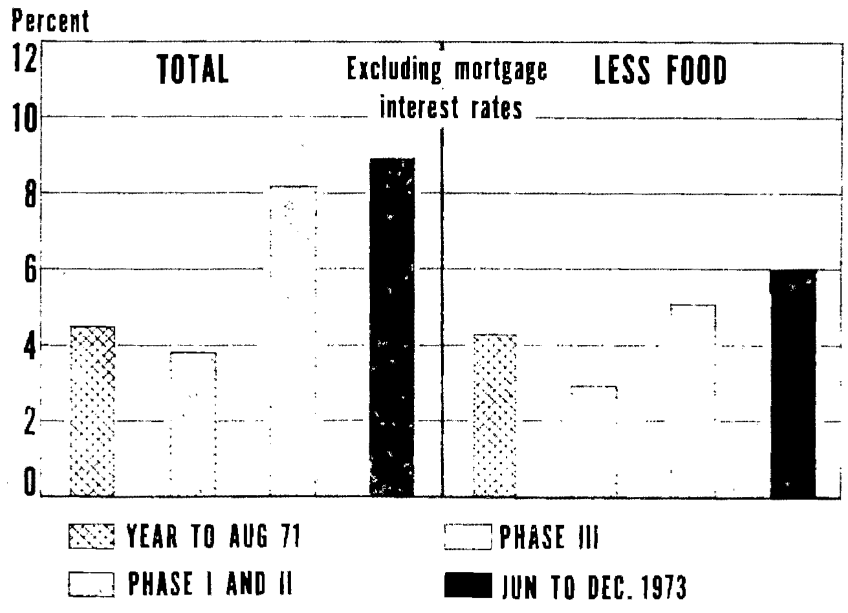

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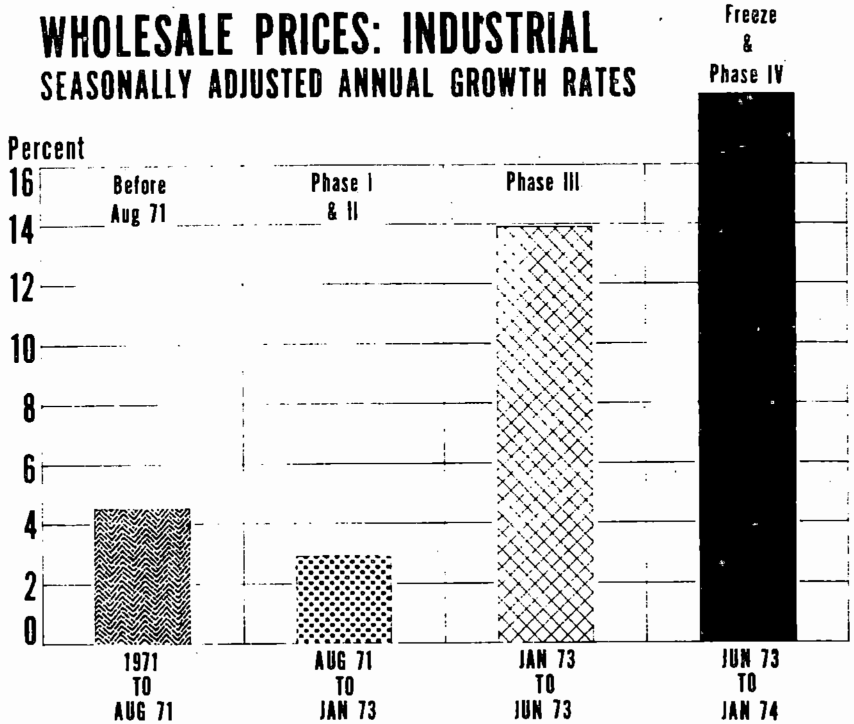

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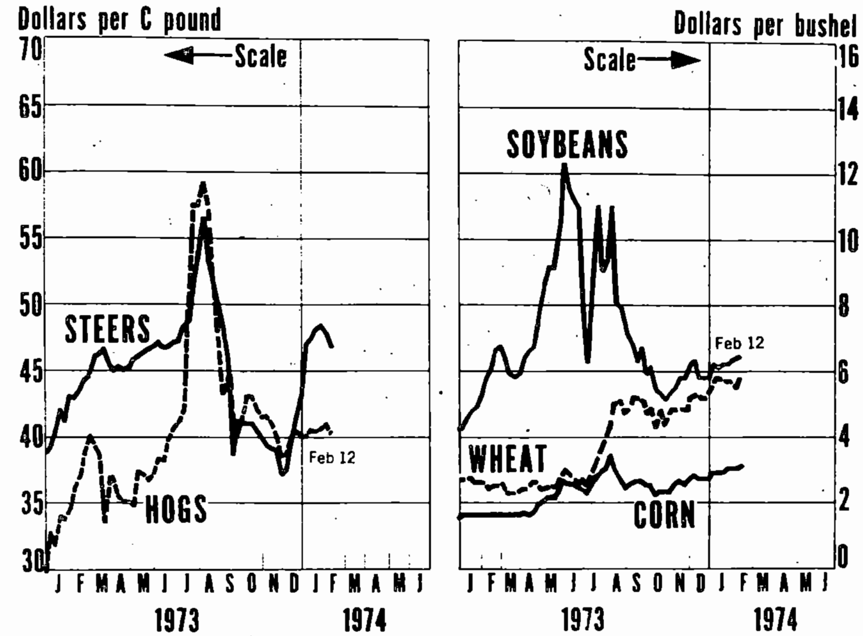

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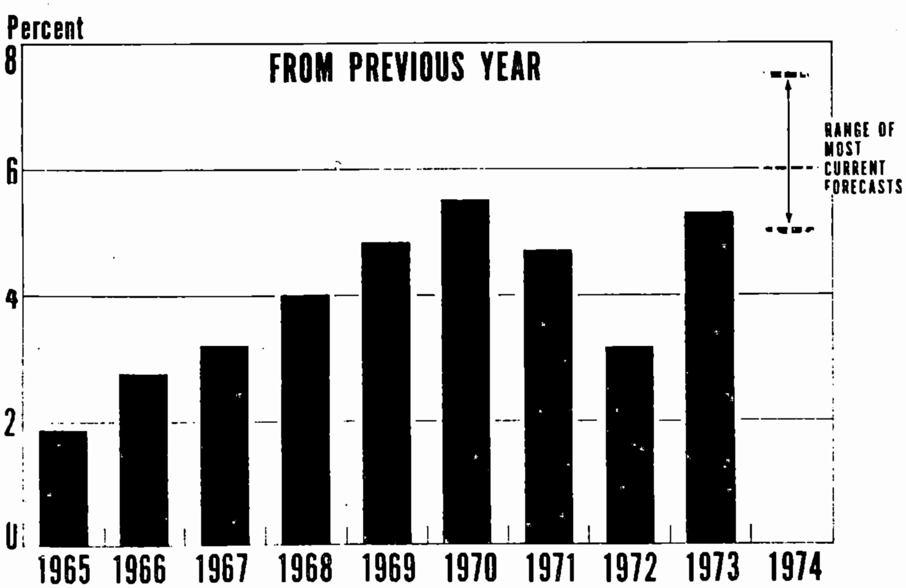

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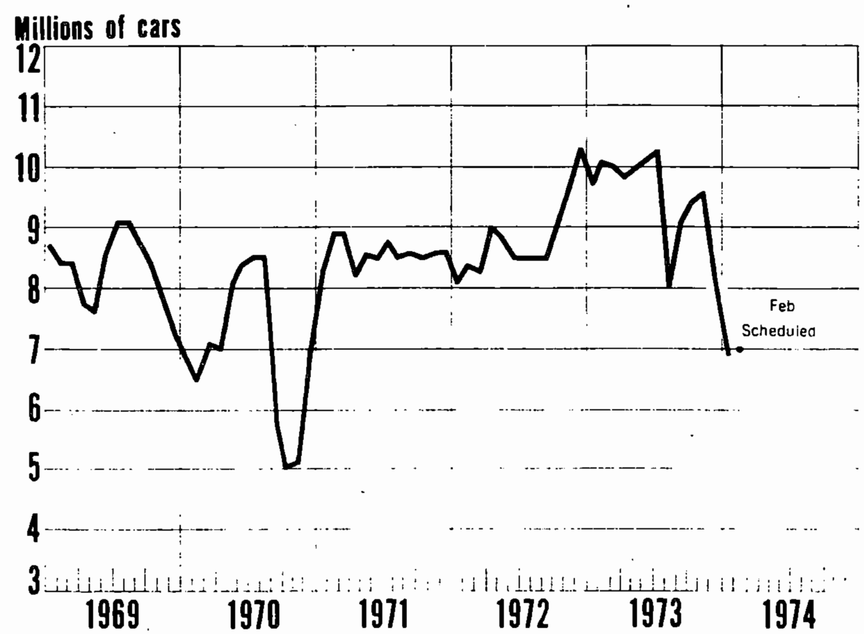

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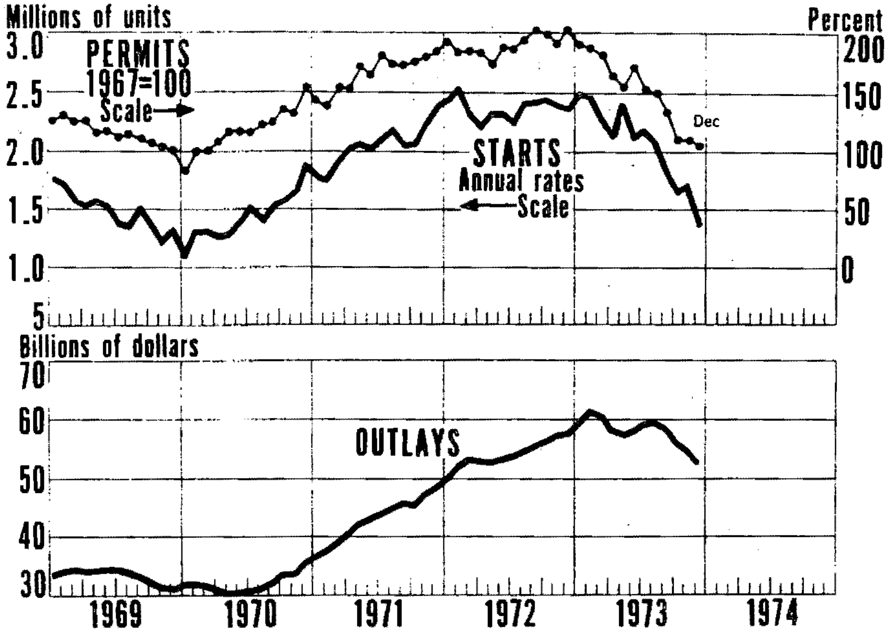

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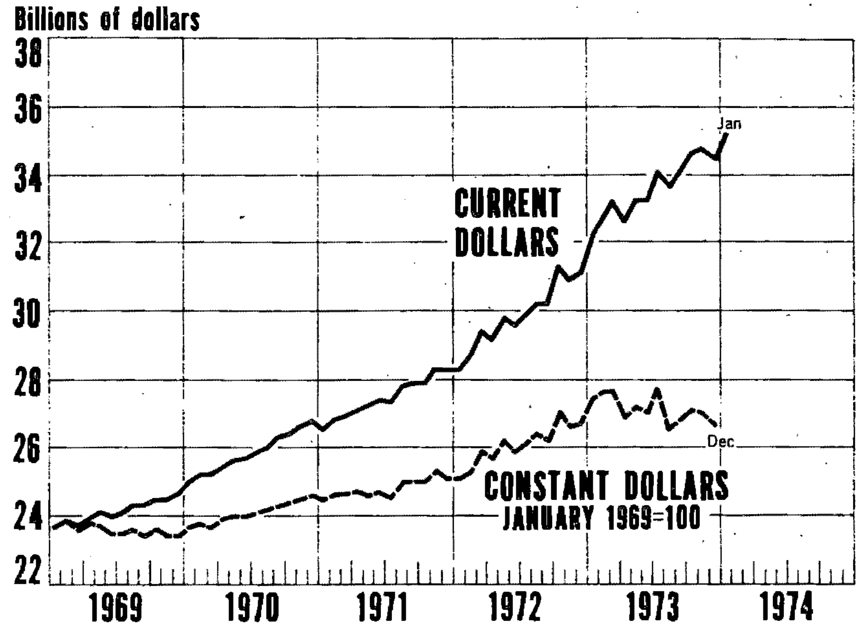

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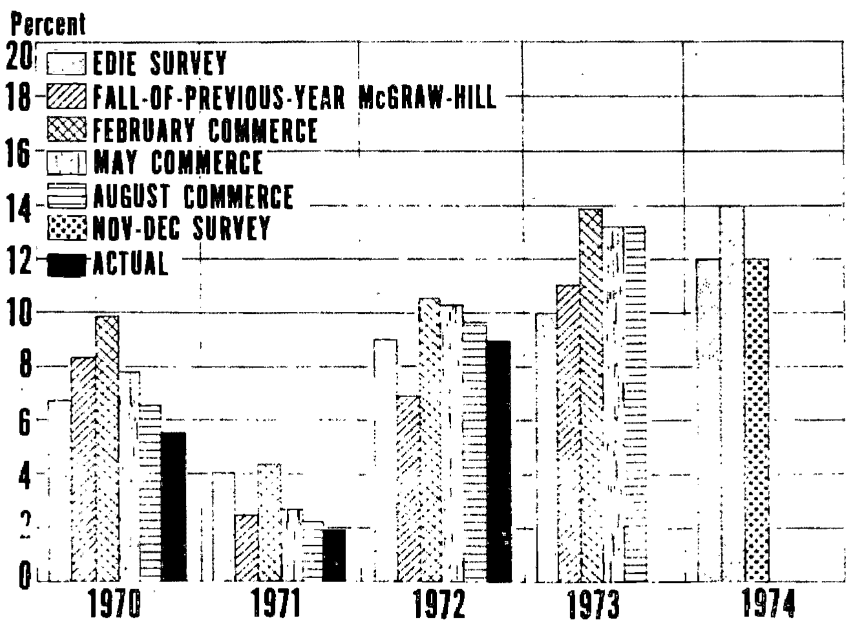

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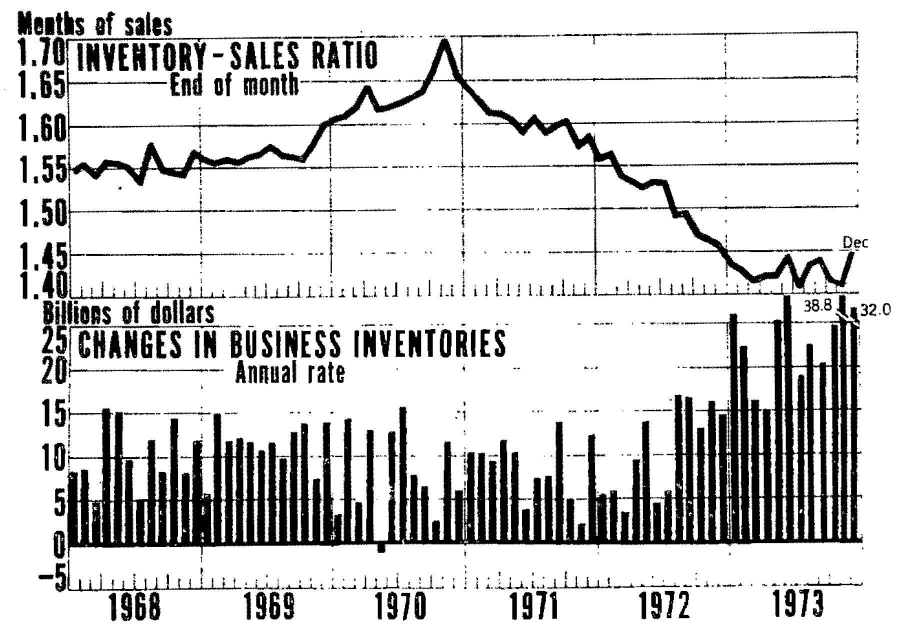

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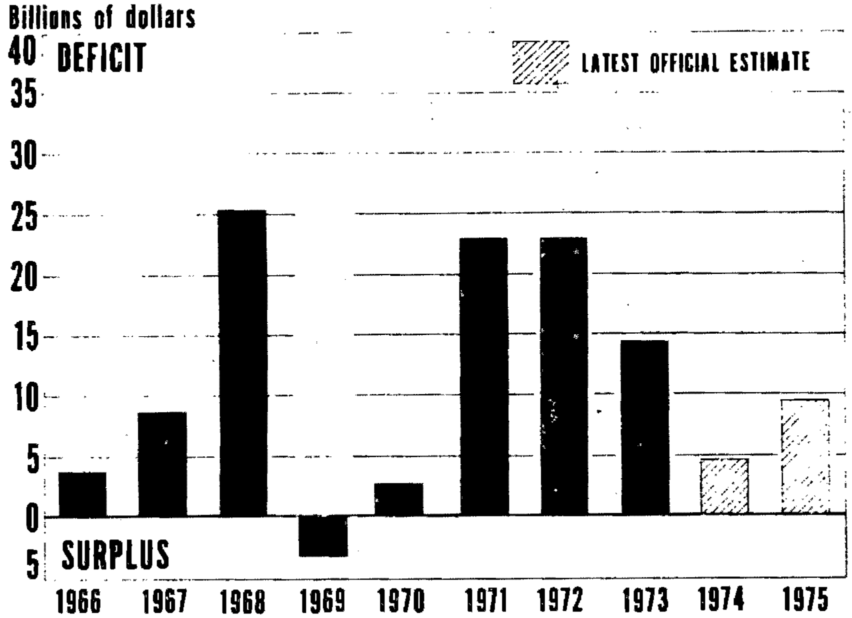

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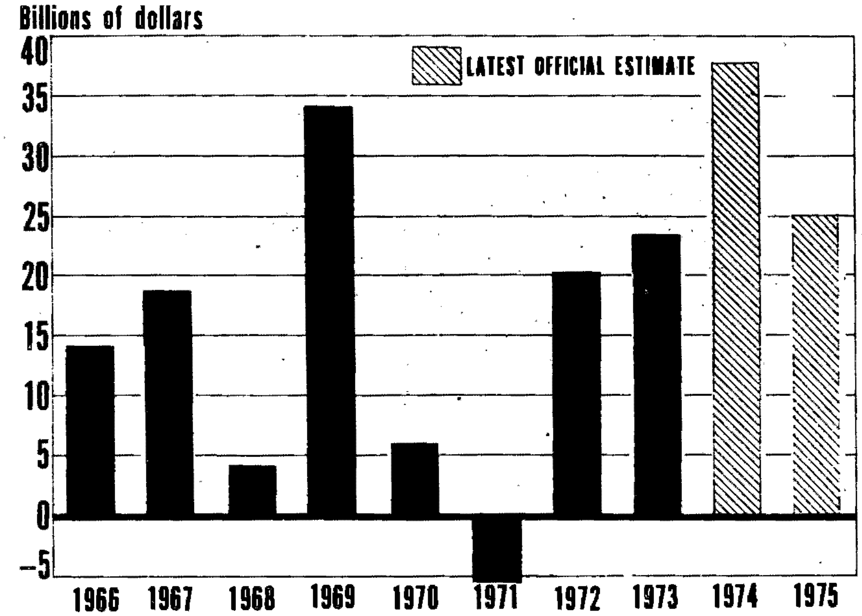

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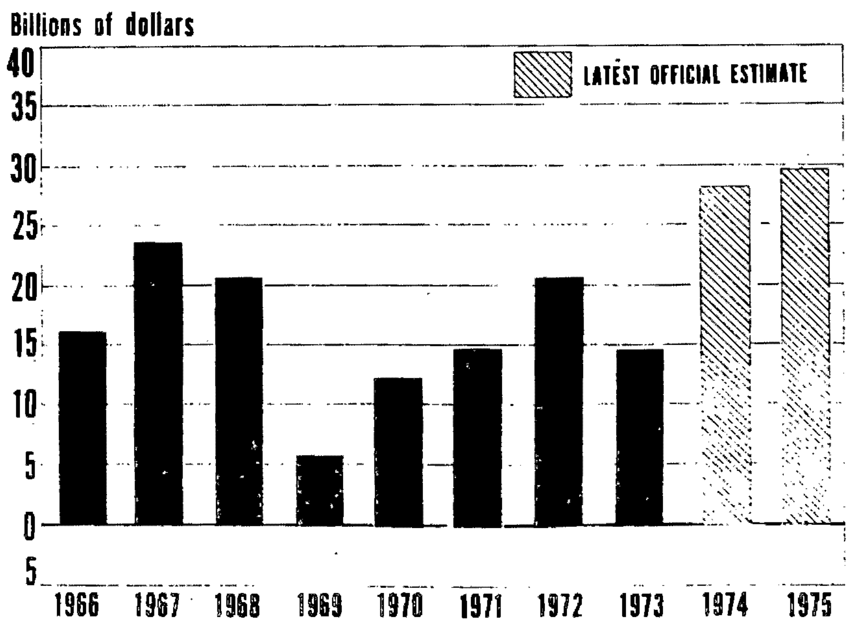

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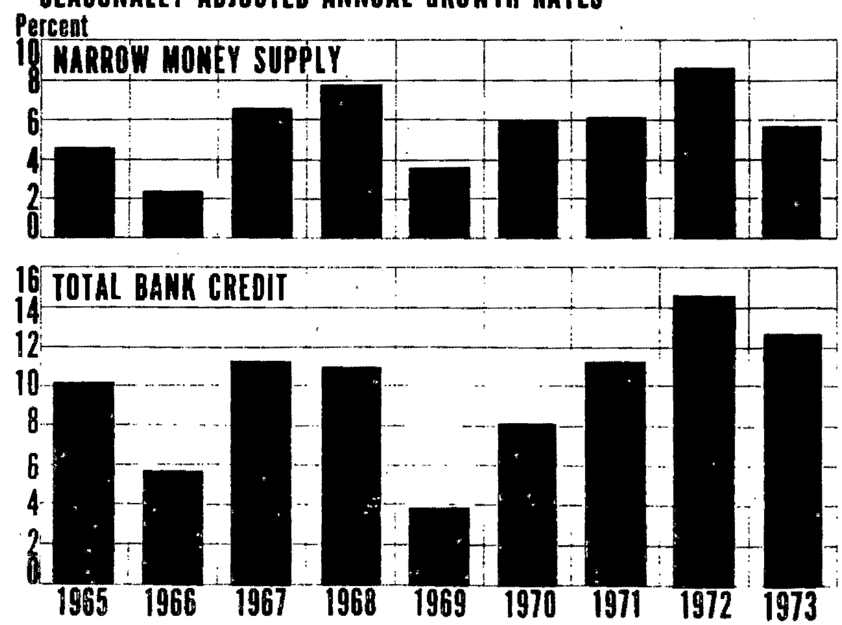

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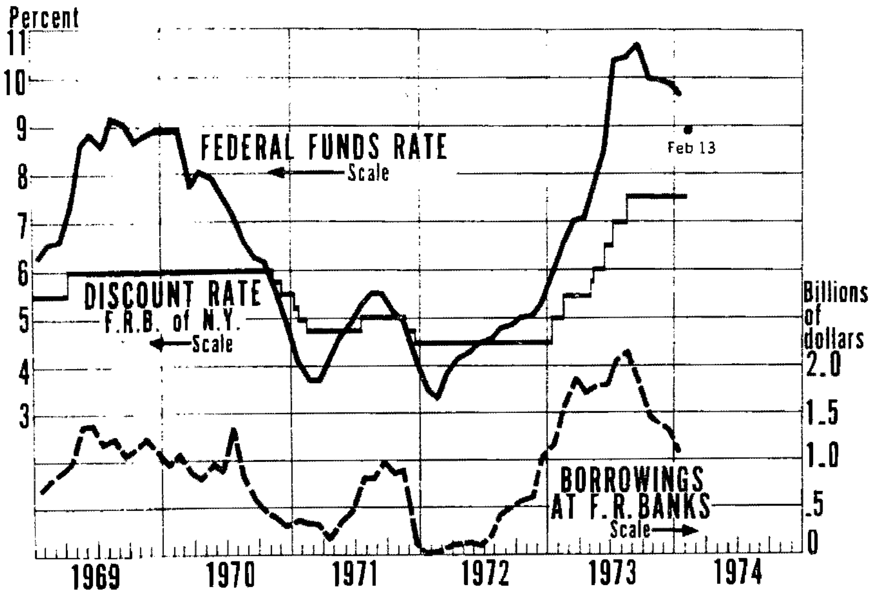

M1: NARROW MONEY SUPPLY, FROM 3 MONTHS EARLIER

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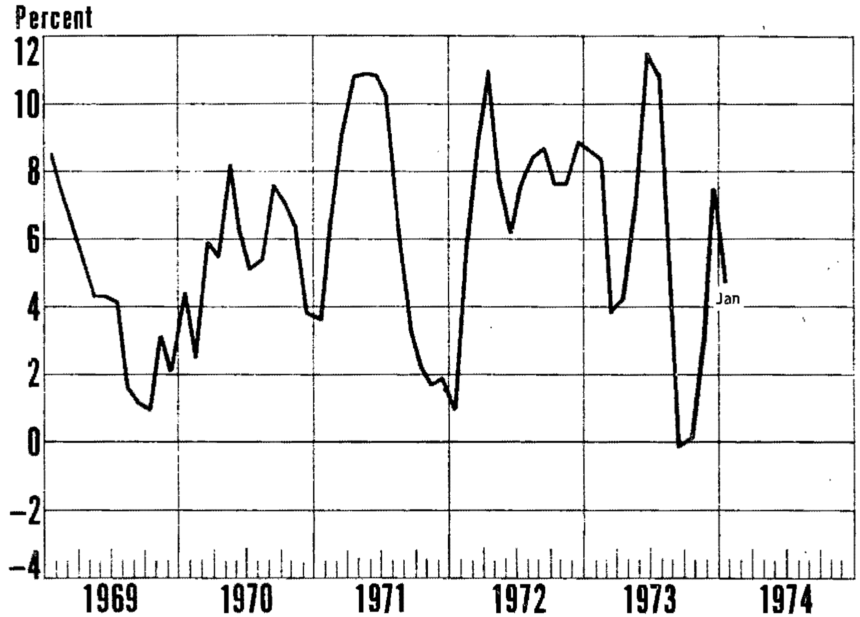

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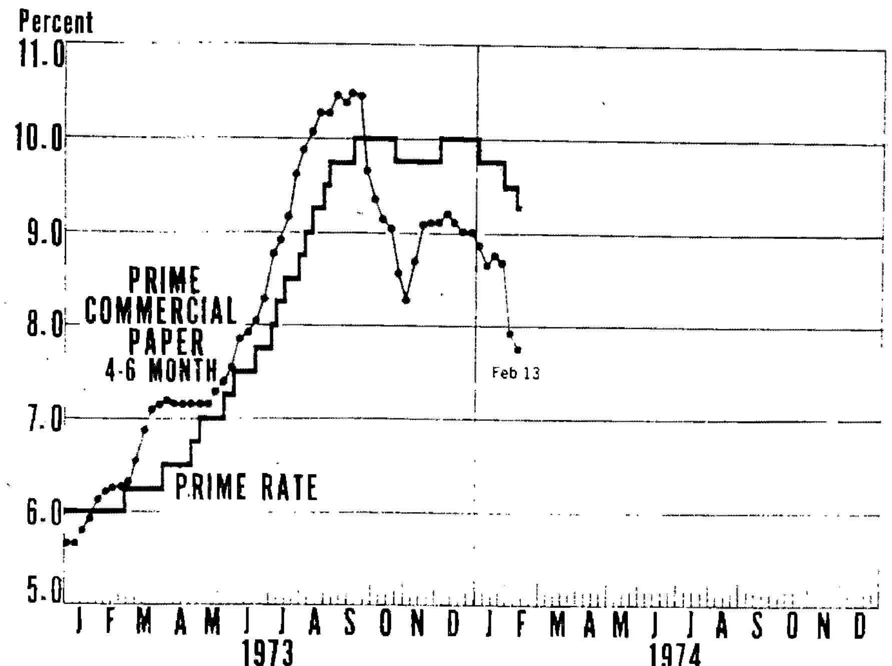

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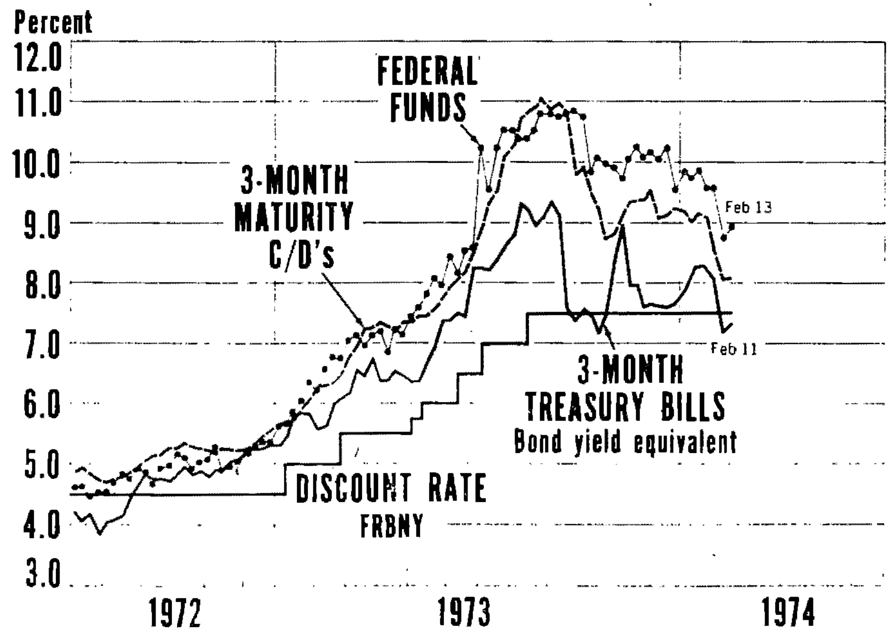

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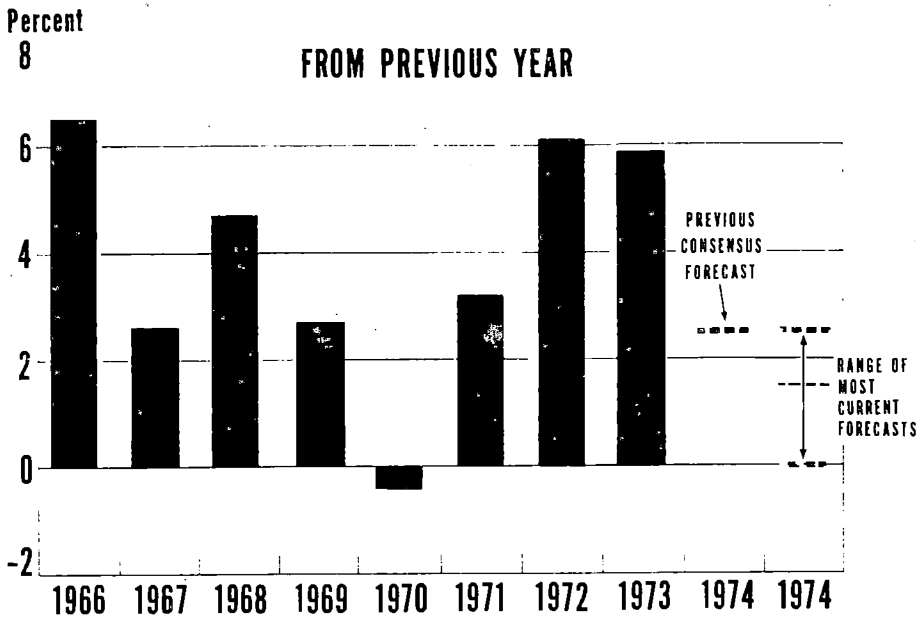

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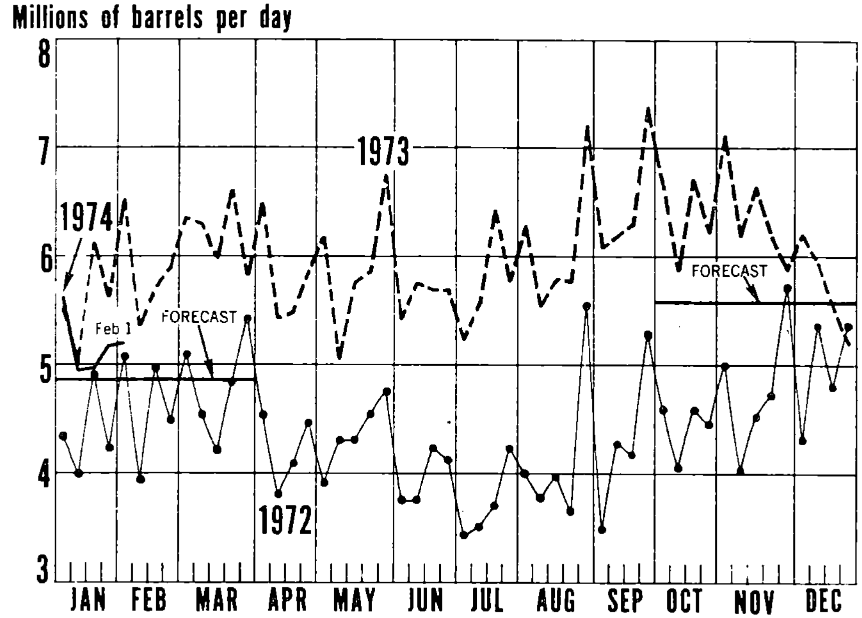

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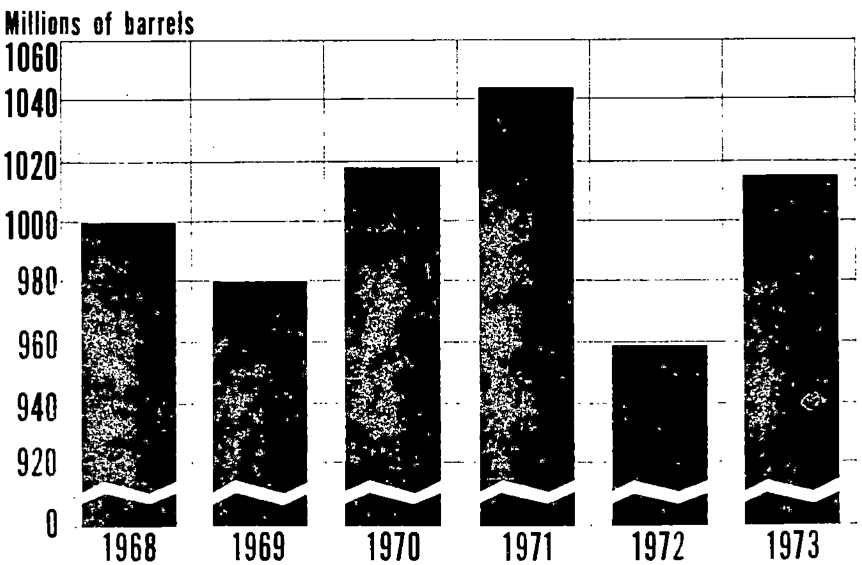

Source: Bureau of Mines.

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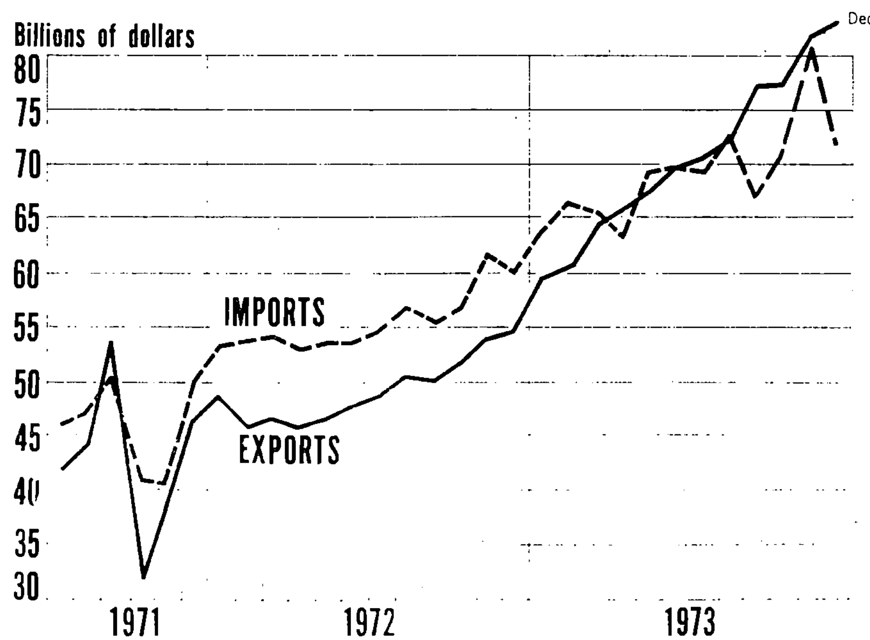

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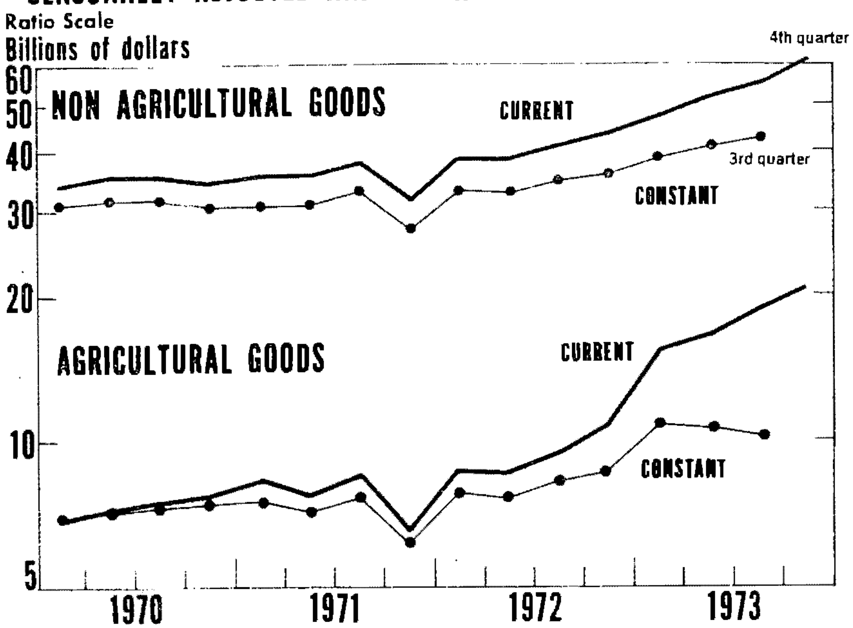

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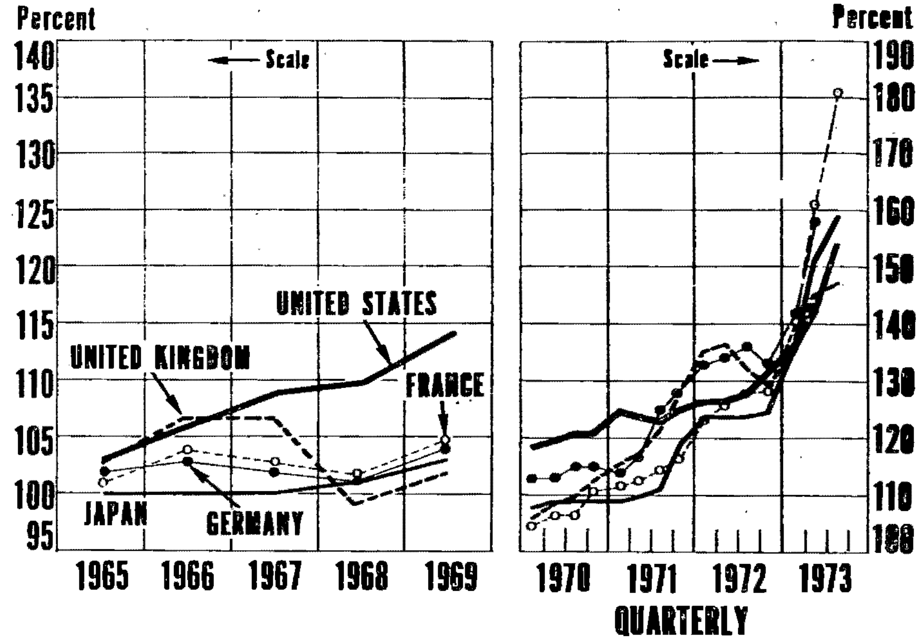

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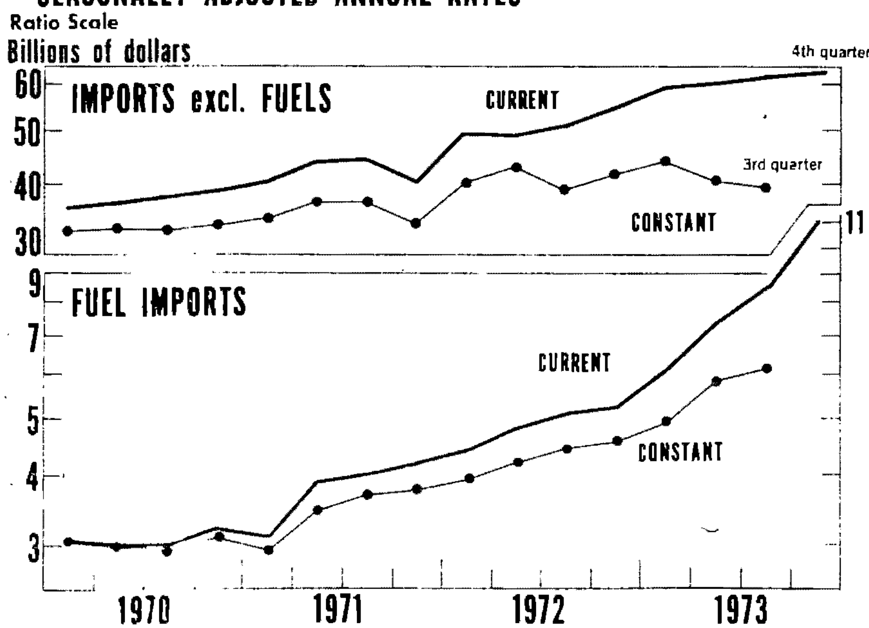

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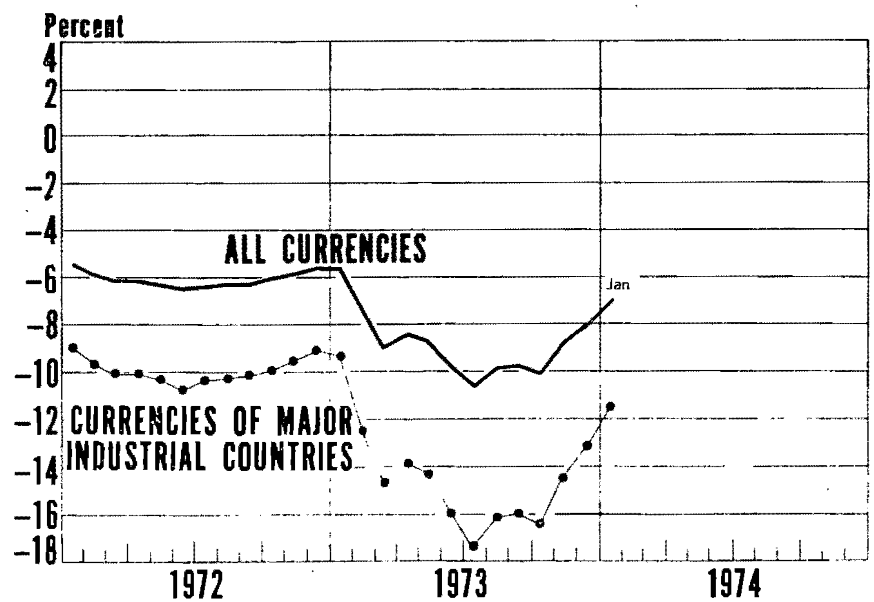

FEDERAL RESERVE

press release

For Immediate Release November 13, 1973

Dr. Arthur F. Burns, Chairman of the Federal Reserve Board, issued the following statement upon his return from a meeting of central bankers in Europe:

> The Governors of the central banks of Belgium, Germany, Italy, the Netherlands, Switzerland, the United Kingdom, and the United States at the November meeting held in Basle, Switzerland, discussed the agreement with regard to official gold transactions reached in Washington on March 17, 1968, and decided that the agreement should be terminated.

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For release on delivery

Statement by

Arthur F. Burns

Chairman, Board of Governors of the Federal Reserve System

before the

Subcommittee on International Finance

of the

Committee on Banking and Currency

House of Representatives

December 5, 1973

I am pleased to appear before this Committee to discuss recent developments in foreign exchange markets and in the balance of payments.

This year has been characterized by alternating periods of turbulence and stability in exchange markets. You will recall that, following several weeks of severe disturbance in exchange markets, the dollar was devalued for a second time on February 12. At that time, Italy and Japan chose to float their currencies, thus joining the Canadian dollar, British pound, and Swiss franc -- which were already floating. New pressures in exchange markets developed in late February and early March, and led to a further extension of floating among major currencies.

Over the next two months, the average dollar price of 10 major currencies (those of Japan, Canada, and 8 European nations) stabilized at a level some 20 per cent above the exchange parities that prevailed in the spring of 1970. In mid-May, however, the dollar again began to decline sharply, so that by July the average dollar price of these 10 currencies increased an additional 10 per cent.

This further substantial depreciation of the dollar did not seem consistent with international price levels or with longer-term prospects for our balance of trade or payments. Moreover, fluctuations of exchange rates from day to day and hour to hour had become more pronounced. In these circumstances, and after full consultation with the Treasury and representatives of other countries, the Federal Reserve began on July 10 to intervene in the exchange market. Through the month of October, the System sold a total of $512 million of European currencies, mainly German marks, drawing on the swap lines to finance this intervention. By the end of that month, enough marks, French francs, Belgian francs, and Dutch guilders were purchased in the market to repay in full these earlier swap drawings.

After our intervention in July and the release of favorable U.S. trade and payments figures, the dollar strengthened by about 3 per cent during the first weeks of August. There was little further change in the dollar's value until late October, at which time the announcement of a large trade surplus for September triggered another sharp advance. In recent weeks the dollar has strengthened further in relation to the major European currencies and the Japanese yen. The appreciation of the dollar against the yen would have been even greater if the Bank of Japan had not intervened in the market by making large sales of dollars. By the end of November, the average dollar price of the ten major currencies mentioned earlier had returned to the level that ruled between mid-March and mid-May; in other words, it was again some 20 per cent above the exchange parities prevailing in the spring of 1970 -- or slightly above the level in the week following the February 12th devaluation.

Some market observers have pointed to anticipations of the impact of oil restrictions by Arab countries as a factor contributing to these developments in recent weeks. Others have cited the stabilizing effects of official intervention by the Federal Reserve and other monetary authorities. There is no doubt in my mind, however, that the basic factor has been the decisive turnaround in the U.S. balance of payments. New evidence of this fundamental improvement in our payments position has been accumulating with each passing month.

Our exports have been rising at an extraordinary rate this year. Measured in current dollars, exports in the third quarter were 47 per cent above their level in the third quarter of 1972. Much of this increase is accounted for by rising prices.

But even in real terms, exports grew 23 per cent over this period. The big increase in our agricultural exports -- from an annual rate of $9-1/2 billion in the third quarter of 1972 to some $19 billion in the third quarter of this year -- has received a great deal of publicity. It is less often appreciated that non-agricultural exports, which account for about three-fourths of our total exports, have been expanding at extra-ordinarily rapid rates as well.

Part of the strong showing of exports is attributable to last year's poor harvests abroad and the current world-wide industrial boom. But the improvement also reflects a lesser rate of inflation in the United States than in other industrial countries and, far more important than this, the cumulating effects of the depreciation of the dollar since 1971.

The changes in our international competitiveness resulting from the depreciation of the dollar are having an effect on our imports as well as on our exports. In real terms, imports actually declined between the first and third quarters of this year, despite the strength of domestic demands.

The value of imports did increase at an annual rate of 14 per cent during that period, but only because of increases in their dollar price.

As a result of these developments, the trade balance has moved from a deficit of nearly $7 billion in 1972 to a surplus at an annual rate of $3 billion in the third quarter of this year. The trade balance continued to be in surplus at a substantial rate in October. It therefore now seems likely that the United States will have a trade surplus, albeit of modest size, for 1973 as a whole.

The balance of international flows of long-term private capital has also moved in our favor this year. Outflows of capital have moderated since the first quarter and are estimated to have slowed sharply in the third quarter. Prior to the recent decline in stock market prices, renewed confidence in the dollar helped to stimulate foreign purchases of American securities. Foreign direct investment in this country has also been substantial this year. These developments reflect, among other factors, the improved profitability of producing internationally traded goods within the United States relative to production abroad.

The basic balance -- that is, the aggregate of all current international transactions and long-term capital flows -- has been strengthening throughout this year. The improvement in the third quarter was dramatic enough to produce a large surplus -- the first quarterly surplus we have experienced since 1969. Net flows of short-term capital have also been favorable to the United States since the first quarter. As a result, the official settlements balance was actually in surplus during both the second and third quarters. Preliminary data for October and November suggest that the surplus has continued into the present quarter.

Short-term prospects for the balance of payments have become clouded, however, by recent developments in the oil situation. The price of our oil imports has risen spectacularly, from an average of $2.75 per barrel in the first quarter of 1973 to over $5.00 currently. The boycott by Arab producers has begun to reduce our petroleum imports and, if continued, would reduce our imports next year by some 3 million barrels per day below the amount that had been expected to be available. Even so, in view of the recent sharp price increases, our total payments for oil imports in 1974 would probably exceed by a substantial margin the $8 billion paid in 1973. Of course, if world trade in oil were to resume a more normal pattern at these astronomic prices, the cost of our oil imports would rise still more steeply. However, the net impact on our overall balance of payments would be substantially less or could even be favorable, since a good part of the increased payments for oil by the United States and other countries would find its way back to this country, directly or indirectly, in the form of increased exports, or capital inflows, or income receipts.

Whatever effects the oil shortage may have on our balance of trade and payments, a more immediate concern is the impact on domestic production and employment. A reduction in imports of crude oil and petroleum products by 3 million barrels per day amounts to a shortfall of more than 15 per cent from estimated demands for this source of energy. Only a small part of this shortfall could be made up during 1974 by increased domestic output of crude oil, or by substitution of other fuels for petroleum products. In the short-run, there are only limited possibilities for substituting other fuel for oil in industrial plants, or for altering techniques of production in ways that reduce dependence upon petroleum products.

The President's program to conserve fuel recognizes this basic fact, and is therefore oriented toward economizing end-product uses -- such as reduced consumption of gasoline in passenger cars, and reduced amounts of oil for heating homes and commercial and industrial buildings. To keep the oil shortage from generating major economic dislocations, our citizens will have to go to some trouble and put up for a time with various inconveniences. There is no practical alternative for the immediate future if seriously adverse effects on production and employment are to be avoided.

At best, a prolonged embargo on Arabian oil shipments to the United States will result in some economic dislocation next year. The demand for new cars, for tires and other auto parts, for suburban housing, for recreational vehicles, for restaurant meals and other travel-related expenditures will be adversely affected; commercial airlines will reduce their purchases of jet aircraft; and fewer motels and vacation homes will be constructed. These developments will be offset in part by larger activity in other trades -- ranging from coal to blankets and sweaters, and from drilling machinery to bicycles and buses. Our inflationary problem, meanwhile, will be aggravated by rising gas and oil prices.

The situation in which we find ourselves is obviously very difficult, but I believe it is manageable. The underlying strength and resilience of our economy must never be underestimated. Capital spending plans of business remain strong, and so are inventory demands for a host of materials and components that have been in short supply for many months. Our principal asset -- the resourcefulness of the American people -- remains entirely intact. As 1974 moves on, I would expect the domestic output of crude oil to gradually increase, electric utilities to shift to greater use of coal, auto manufacturers to concentrate more of their production on the smaller cars demanded by consumers, and other adjustments to be made in the thousands by ingenious businessmen across the land.

The longer-run economic implication of the cutoff of Arabian oil supplies should not leave us in any doubt. The United States can no longer afford to lose time in working towards an independent ability to meet its energy requirements. We must now move forward with determination on many fronts -- nuclear energy, solar energy, coal conversion, exploration for oil. Recent events should teach us that, even with a relaxation of the current boycott, we cannot remain so heavily dependent on oil supplies from foreign nations.

Some months will need to elapse before the long-run implications of the oil problem for our balance of payments clarify. So far at least, the restrictions on oil supply appear to have strengthened the world's confidence in the dollar. But even before the Middle East conflict erupted, the dollar was viewed with renewed esteem. The dollar is again a strong currency, and we can expect further support to our foreign trade and payments from the lagged effects of past exchange-rate changes.

Continued strength in the balance of payments will require, however, a satisfactory domestic price performance relative to other countries. A year or two ago our rate of inflation was substantially lower than that of other industrial countries. Unfortunately, a large part of this margin of competitive advantage has eroded in recent months. In October, the consumer price index was 0.8 per cent above September, and 7.9 per cent above October 1972. Clearly, the dangers of inflation remain very much with us. At the same time, as I have already noted, the oil shortage will cause shifts in the structure of industry and have adverse effects on overall production and employment. Economic policy in the months ahead thus faces the extremely difficult task of contributing to the objective of regaining price stability, while at the same time minimizing the risks of any extensive weakening in economic activity.

In the remainder of my comments this morning, I would like to share with you my impressions of the recent evolution of the world monetary system.

In the past several months, a large number of economic, political, and military events occurred that had potentially disruptive implications for exchange markets. Despite these disturbing events, orderly market conditions and general stability have prevailed. The official intervention that was undertaken has given us helpful experience in managing a system with exchange-rate flexibility in a way that preserves orderly markets without frustrating desirable adjustments. Although I remain skeptical of the long-run viability of a floating exchange rate regime, this experience supports the continuance of the present exchange-rate arrangements for the immediate future.

For the longer run, we must rely more heavily on rules of international law in the monetary area. Such a reform is the objective of the Committee of Twenty, which has been meeting periodically throughout 1973, and will continue its work into 1974. Considerable progress in clarifying issues has already been made, as evidenced by the Nairobi report of the Chairman of the Committee of Twenty and the associated First Outline of Reform presented by the Chairman of the Committee's Deputies. I expect further clarification and further convergence of national views in coming months.

But it is important to avoid unrealistic expectations. Some of the reform issues are extremely difficult, progress in reaching agreement will continue to be gradual, and new developments may cloud the situation -- as the energy issue has done in recent weeks.

Moreover, I have in recent months come to think of international monetary reform as an on-going, evolutionary process -- not just as the final outcome of formal negotiations. In view of changing objective circumstances and continuing divergence in some official views, it is hardly practical to think of monetary reform in terms of a finished blueprint that is to be implemented in its entirety some morning after a final meeting of the world's finance ministers and central bank governors. Even while discussions continue in the Committee of Twenty and other forums, it is both possible and desirable to adjust some parts of our international financial machinery.

One such step in this evolutionary process has been the recent termination of the March 1968 agreement with regard to official gold transactions. That agreement, which established the so-called two-tier gold market, was born of the 1968 gold crisis. Developments in the private gold market were then threatening to undermine the international monetary system by draining it of gold -- which at the time was the world's principal reserve asset. To deal with this difficulty, the central banks of Belgium, Germany, Italy, the Netherlands, Switzerland, the United Kingdom, and the United States agreed that they would no longer buy or sell gold in the private market.

In view of the suspension of convertibility of dollars into gold since August 1971, the 1968 agreement had become an anachronism. Its termination removes an obstacle to official sales of gold in the private market, and will thus permit greater flexibility of action in the future. Official sales of gold can be useful in preventing wide fluctuations in the gold market that at times generate instability in currency markets.

In due course, the United States and other countries will make decisions about possible sales in the gold market. In doing so, our government will comply fully with Article IV, Section 2 of the IMF Articles of Agreement. That Article states in essence that no member of the IMF shall sell gold below its official price or buy gold at a price above its official price. I am confident that most, if not all, foreign governments will also respect this Fund Article. Hence, while they may sell gold, which now fetches a price in the market that is far above the official price, they will not buy gold either from the market or from each other in the foreseeable future.

The termination of the 1968 agreement will make possible a further reduction in the role of gold in the international monetary system. With the establishment of the SDR facility, which was not available in 1968, we now have an alternative primary reserve asset. It has therefore become practical to consider steps that may gradually move gold out of official reserves.

Policy with regard to intervention in exchange markets is another area in which progress is beginning to be made in the evolution of the international monetary system. Under present exchange-rate arrangements, authorities of major countries are consulting and cooperating as they make decisions on intervention. This experience, and the experience to be gained in coming months, will be of great value in the effort to establish more formal exchange-rate arrangements for the longer-run future.

At the present time, with many currencies floating in relation to the dollar, official holdings of U.S. dollars will only be reduced through market intervention by foreign central banks. A substantial reduction of dollars presently held in foreign official reserves -- the reserve liabilities of the United States amount to some $70 billion -- is clearly desirable as a long-run objective. Progress in this direction has been most marked in the case of Japan, where dollar reserves have declined sharply in recent months. At the end of November, Japanese official reserves were reported to be some $6 billion below their level at the end of February. It would be desirable for other countries with excess reserves also to sell dollars gradually when market forces are serving to appreciate the dollar substantially against their currencies.

The controls imposed on capital flows may be a third area of international monetary arrangements where evolutionary steps can be taken. Starting with the measures adopted in 1963 and expanded in 1965, our government has administered a system of restraints on capital outflows in order to protect the balance of payments and avoid disturbance to international markets. These measures -- the interest equalization tax, the foreign direct investment regulations, and the voluntary foreign credit restraint guidelines -- have been adapted over the years to changing economic conditions, but it has been the objective to remove them when they were no longer necessary. Other countries have similarly imposed new controls, or tightened existing controls, to deal with capital flows considered to be temporary or reversible.

Early this year, the Administration announced its intention to phase out our controls by the end of 1974, but noted that the timing of liberalizing steps would depend on balance-of-payments developments. In view ot the recent strengthening of the balance of payments, it may be feasible for the agencies administering the controls -- the Treasury Department, the Department of Commerce, and the Federal Reserve System -- to move forward over the coming months with an orderly reduction of those restraints. Similarly, it may prove feasible for other countries to relax some of their earlier-imposed restraints on capital inflows.

In conclusion, I would like to note once again that the strengthening of our balance of payments and the restoration of confidence in the dollar in exchange markets stand out as this year's major economic achievements. These developments have served to bolster confidence in our nation's future at a time when we have been besieged with all sorts of unhappy economic and political news.

In fact, these foreign exchange developments have transformed the atmosphere in which international financial problems are being discussed. We no longer hear voices from abroad about inflation being exported from the United States. There is no longer so much complaining about a world flooded with dollars. Even complaints about the "dollar overhang" have become muted.

We must, of course, be careful and not exaggerate the extent of the dollar's recovery. There is much unfinished work ahead of us. Nonetheless, it is gratifying to be able to draw your attention to the improvement that has occurred in our balance of payments, and to advise you that the dollar is today a respected currency in financial circles both here and abroad.

Confidence in the dollar is essential both to a healthy domestic economy and to a successful evolution of the international monetary system. Looking to the future, we must strive to conduct all our economic policies -- domestic as well as international -- in such a manner that they will maintain, and indeed strengthen, that confidence.

* * * * * *

July 16, 1973

Dear George:

Thank you for your personal note enclosing copies of the press releases regarding changes in the size of the Federal Reserve swap arrangements.

Yours sincerely,

P.-P. Schweitzer

Mr. George W. Mitchell
Vice Chairman
Board of Governors
Federal Reserve System
Washington, D.C. 20551

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D.C. 20551

OFFICE OF THE VICE CHAIRMAN

July 11, 1973

Dear Pierre-Paul:

You may be interested in the two enclosed press releases regarding changes in the size of the Federal Reserve swap arrangements.

Sincerely yours,

George W. Mitchell

The Honorable Pierre-Paul Schweitzer
Managing Director
International Monetary Fund
Washington, D. C. 20431

Enclosures

FEDERAL RESERVE

press release

For immediate release

July 11, 1973

The Federal Reserve System said today 13 foreign central banks and the Bank for International Settlements were involved in the $6.25 billion swap network increase announced yesterday.

The largest increases, of $1 billion each, involved the Bank of Canada, Bank of France, German Federal Bank and the Bank of Japan.

A swap arrangement is a short-term facility under which the Federal Reserve and another central bank mutually agree to exchange dollars for the currency of the other country up to a maximum amount over a limited period of time.

The increases and the new totals of the swap lines are as follows (in millions of dollars):

Foreign Bank	Increase	Total
Austrian National Bank	50	250
National Bank of Belgium	400	1,000
Bank of Canada	1,000	2,000
National Bank of Denmark	50	250
Bank of England	--	2,000
Bank of France	1,000	2,000
German Federal Bank	1,000	2,000
Bank of Italy	750	2,000
Bank of Japan	1,000	2,000
Bank of Mexico	50	180
Netherlands Bank	200	500
Bank of Norway	50	250
Bank of Sweden	50	300
Swiss National Bank	400	1,400
Bank for International Settlements		
Swiss francs/dollars	--	600
Other European currencies/dollars	250	1,250
TOTALS	6,250	17,980

(Note: The foregoing announcement is also being released by the Federal Reserve Bank of New York)

- 0 -

FEDERAL RESERVE

press release

For immediate release July 10, 1973

The Federal Reserve announced today an increase of $6.25 billion in the reciprocal currency ("swap") arrangements that it maintains with 14 foreign central banks and the Bank for International Settlements. The increase raises the total of the System's swap network to $17.98 billion.

As in the past, the present expansion of the swap network was worked out in full consultation with the Treasury.

A swap arrangement is a short-term facility under which the Federal Reserve and another central bank mutually agree to exchange dollars for the currency of the other country up to a maximum amount over a limited period of time.

This announcement reflects arrangements that are being carried out in conformity with the policy that was agreed to at the March 16th Paris meeting of Finance Ministers and central bank governors.

- 0 -

FEDERAL RESERVE
press release

For immediate release

July 10, 1973

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BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

OFFICE OF THE VICE CHAIRMAN

May 2, 1973

Dear Pierre-Paul:

How thoughtful of you to write with respect to my resignation from the Board. I am very grateful to you.

I hope that our paths will cross again before you leave the Fund in order that I may have the opportunity to tell you in person how much I appreciate both my personal contacts and your great contribution to the International Monetary System. As a matter of fact, I wish you were remaining on at the Fund indefinitely.

With many thanks and warm regards, I am

Sincerely,

JLR

J. L. Robertson

The Honorable Pierre-Paul Schweitzer
Managing Director
International Monetary Fund
Washington, D. C. 20431

April 24, 1973

Dear Jim:

I was sad to learn that you will be leaving the Board of Governors at the end of the month, although I would be the first to admit that, after forty-six years, you have more than earned a respite from public service.

Though the opportunities which we in the Fund have had to work directly with you have been limited, we have always been conscious of your wise and friendly influence at the Board. We have valued your guidance and advice when the occasion arose to seek your counsel.

May I take this opportunity to wish you every happiness and good fortune in whatever future activity you choose to take up.

With warm personal regards,

Yours sincerely,

P.-P. Schweitzer

Governor James Louis Robertson
Vice Chairman
Board of Governors
Federal Reserve System
Washington, D. C.

FEDERAL RESERVE

press release

For immediate release April 19, 1973

Governor James Louis Robertson, Vice Chairman of the Board of Governors of the Federal Reserve System, today announced that on March 29, 1973, he submitted his resignation to President Nixon, to become effective no later than the end of April.

His letter addressed to the President was as follows:

"Dear Mr. President:

"I hereby tender my resignation as a member of the Board of Governors of the Federal Reserve System, effective as of the close of business April 30, 1973, or any earlier date that might better suit your convenience.

"Needless to say, I deeply appreciate the opportunity and privilege of serving the public during so many different Administrations - nearly forty-six years in the federal public service, over twenty-one years as a member of the Board of Governors, and a third of that period as its Vice Chairman.

Sincerely,

J. L. Robertson"

While he intends to remain active, Governor Robertson said he has not made any plans and will not do so until after he leaves office.

- 0 -

No Reply -

March 15, 1973

Dear Arthur:

This is to acknowledge receipt of the advance copy of this year's Prelude to the Annual Report of the Board of Governors of the Federal Reserve System. I am sure that we will find the document very stimulating and am looking forward to receiving in a few weeks the complete Report covering Federal Reserve operations during 1972.

Sincerely yours,

Pierre-Paul Schweitzer

Mr. Arthur F. Burns
Chairman of the Board of Governors
Federal Reserve System
Washington, D.C. 20551

CHAIRMAN OF THE BOARD OF GOVERNORS
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

March 23, 1973

Accept

Dear Mr. Schweitzer:

I cordially invite you to join me and the other Members of the Board of Governors for dinner on Monday, March 26 at 8:00 p.m. at the Federal Reserve Building (business suits).

We shall appreciate your letting us know whether or not you can be with us (737-1100, Extension 3324).

Sincerely yours,

Arthur F. Burns

The Honorable Pierre-Paul Schweitzer
Managing Director
International Monetary Fund

Files
Mr. Beza

CHAIRMAN OF THE BOARD OF GOVERNORS
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

March 13, 1973

The Honorable Pierre-Paul Schweitzer
Managing Director
International Monetary Fund
Washington, D.C.

Dear Pierre-Paul:

The Board of Governors is publishing separately again this year that part of its Annual Report dealing with monetary policy and the economy in the thought that many may find it useful to have this material in advance of the full Annual Report.

I am enclosing an advance copy of this Prelude to the Fifty-Ninth Annual Report of the Board of Governors of the Federal Reserve System on "Monetary Policy and the U.S. Economy in 1972" which I hope will be of interest to you. The complete Report covering operations during the calendar year 1972 will be available within the next several weeks, and will be sent to you at that time.

Sincerely yours,

Arthur F. Burns

Arthur F. Burns

Enclosure (w/ Mr. Del Canto)

RECEIVED
MAR 14 1973
3:30
Western Hemisphere Department

Mr. Schweitzer

INTERNATIONAL MONETARY FUND
WASHINGTON, D.C. 20431

CABLE ADDRESS
INTERFUND

April 17, 1972

MEMORANDUM FOR FILES

Subject: Meeting With Chairman Burns and Other Federal Reserve Officials

On April 13, 1972, Messrs. Polak, Beza, and Crow met with senior officials of the Federal Reserve at lunch; Mr. Dale also attended. Those present from the Federal Reserve were: Chairman Burns and Governors Robertson and Daane; Messrs. Holland, Solomon, Partee, and Bryant of the Federal Reserve staff; and Mr. Coombs of the Federal Reserve Bank of New York.

Chairman Burns began by focusing his attention on the statement delivered by Mr. Polak nine days earlier at the concluding meeting of the U.S. consultation discussions. Chairman Burns said he had not read the statement in its entirety, but that he had read the paragraphs on monetary policy that had been drawn to his attention by his staff. He said, rather angrily, that our understanding of Federal Reserve policy based on the late-1970 consultation discussions--to which reference was made in the statement--was not recognizable to him. Mr. Polak pointed out that we had recorded what we thought was Federal Reserve policy, and Mr. Partee, a senior representative of the Federal Reserve in the consultation discussions, confirmed that our description was based on the presentation he had made in the 1970 consultation discussions.

Chairman Burns then turned his fire on our recommendation that a fairly steady monetary path ought to be maintained and that this year it ought to be at the low end of the range consistent with the desired expansion of demand. In a heated manner, he asked what business it was of a Fund mission to concern itself so deeply with the techniques of monetary management. He thought we should confine ourselves to judgements that monetary policy had been "too tight" or "too loose", and so on, and not to try to tell the monetary authorities how to do their job. He also noted, which perhaps in part explains his agitation, that this question of techniques was a "controversial subject".

Mr. Polak replied to these remarks by observing that if the Fund was to play a role in international monetary management, a task that was assigned to it, it was proper that it probe how countries ran their monetary policies and to make recommendations in this respect. This was done in consultation discussions with countries and in numerous other ways, and he gave examples of the kinds of problems, citing the U.K. and France, we had grappled with in this area. He explained that our present recommendation for U.S. monetary policy had been made in the spirit of trying to further monetary policy coordination among countries. He went on to ask what the Federal Reserve thought were the viable alternatives for achieving such coordination, and although this question was raised from a number of angles, Chairman Burns did not address himself to it.

Rather, he turned to an attack on the notion of a monetary target, characterizing it as too simple minded. He said he lived in a multi-variable world and had to respond to a complex array of situations. A simple monetary rule would not do; we agreed that a more refined monetary rule might be more appropriate. We asked the Chairman how we should characterize Federal Reserve policy, and he replied that the answer had been spelled out in his testimony to the Joint Economic Committee and the latest Annual Report of the Federal Reserve. Mr. Polak said we had read these documents, and intimated that they did not give us a clear view on monetary policy, particularly when trying to look ahead. Chairman Burns seemed to take the position that monetary policy would do whatever was necessary without further specification,although in response to a direct question, he stated with great emphasis that there was no ground for an aggressive monetary policy in present circumstances. (We know from the kind of work the staff of the Federal Reserve does and submits to the Federal Reserve Board, and from the minutes of the Board's meetings, that U.S. monetary is not quite so much at sea as was indicated by Chairman Burns. Perhaps his remarks reflected a strong aversion to being pinned down on policy intentions, and this aversion may have been heightened in view of the controversies on monetary management presently going on within the Federal Reserve)

In any event, Chairman Burns contended, the mission ought to have concentrated its attention on a number of other issues that confront the United States at the present time--issues that he considered more serious and crucial than those pertaining to the conduct of monetary policy. In this connection, he raised questions about the implementation of incomes policy, fiscal policy management, and manpower programs. He was informed by Mr. Polak, and by the Federal Reserve officials who had participated in the consultation discussions, that these topics had received attention and that the weaknesses in these areas had been dealt with in the concluding statement. Chairman Burns commented at length on problems in these areas, indicating his concern over the size of the budget deficit and fiscal trends, expressing his fear that the wage and price controls were not being implemented as effectively as he had hoped, and dismissing the manpower programs as currently run as being a waste of money.

To conclude this discussion, Chairman Burns asked Mr. Polak to summarize the main findings of the mission. Mr. Polak went through the principal points of the concluding statement, and to this Chairman Burns responded that it seemed a fair and balanced assessment. He did not take umbrage, at this stage, to the recommendation for a moderately tight monetary policy, although, as noted earlier, he would not say how such a policy was to be gauged. However, he did take exception to the mission's recommendation that if additional stimulus should turn out to be needed, it be provided through more fiscal expansion. There seemed to be two facets to his reservation on this score: first, there was his general concern that fiscal policy was already too expansionary; and, second price developments may make it unwise to try to achieve as large a demand expansion as has been targeted by the Administration. In this vein, the possible emergence of a fiscal stimulus smaller than had been budgeted--because of shortfalls in spending and overwithholding of taxes--seemed to be welcomed by Chairman Burns rather than being seen as an impediment to the achievement of the employment goal.

The luncheon was concluded with an exchange of views on reform issues on which the Chairman asked for a summary of the sketch (which his staff had given him to read). He did not dissent from the ideas we outlined, and the meeting ended on a pleasant note.

STB

Sterie T. Beza

cc: The Managing Director
The Deputy Managing Director
Mr. Polak
Mr. Gold
Mr. Goode
Mr. Habermeier
Mr. Sturc
Mr. Whittome
Mr. Vera

Office Memorandum

TO : The Managing Director
The Deputy Managing Director

DATE: March 28, 1972

FROM : Fred Hirsch FH

SUBJECT : Federal Reserve Bank of Chicago Symposium on the International Monetary System in Transition

I attended this symposium on March 16-17, and gave the presentation on the background to recent developments which has been put out as DM/72/28. The symposium was basically educational, being designed to bring the mid-Western bankers and businessmen who have been increasingly involved in international commercial transactions into contact with the wider issues in our field. In these terms the conference was a success.

The driving force behind the conference was the Research Department of the Chicago Federal Reserve, and particularly a rather impressive young man called Joseph Kvasnicka.

Analysis and projections of the U.S. balance of payments took up a number of sessions; a striking and rather discouraging feature of the treatment, both by the U.S. officials and by Professor Magee of the University of Chicago, was the concentration on regional and bilateral balances. This produced the familiar focus on the "responsibility" of Canada and Japan in the recent deterioration. Whether or not as a result of this presentation, Mr. Bill Lawson, Deputy Governor of the Bank of Canada, spoke out strongly against this bilateral approach; Canada had come close to balance in its current account, and it was therefore quite unreasonable to expect it to reverse the bilateral improvement that had taken place in its payments with the United States. Mr. Lawson conceded that on this view it would indeed be necessary to find ways of avoiding a net inflow of long-term capital; when asked how this attitude squared with Canada's desire to maintain exemption from the U.S. Interest Equalization Tax and other capital controls, Mr. Lawson hedged publicly, but privately conceded that a revision in Canadian policy on these matters was probably overdue.

The closing address was given by Professor Henry Wallich on "The International Monetary System in the 1970s and Beyond." In fact this consisted rather more of a review of past difficulties, and in the references to future reform, was rather on the negative side. Professor Wallich was not especially enthusiastic about consolidation of dollar balances, beyond saying that this should not be refused if the terms were made especially attractive. As in the case of some other U.S. analysts, such as Fred Bergsten, he takes a definite position that servicing costs should be significantly below the cost of servicing existing U.S. balances, though no convincing rationale is given. Wallich's position on exchange rate flexibility was not fully clear, but the implication seemed to be that this would be a matter for other countries. Wallich emphasized that in the past, the United States had been in the position that major aspects of policy, whether foreign policy or military, had not had to be influenced by an external financial constraint, and he thought it important that this should continue to be the case.

Insofar as these various elements added up to a consistent package, it seemed to me to be an essentially passive policy on convertibility and the exchange rate, combined with a definite view about maintaining competitiveness and the trade balance, implying corrective action by other countries.

cc: Mr. Gold
Mr. Del Canto
Mr. Habermeier
Mr. Sturc
Mr. Whittome
Mr. Polak
Mr. Fleming
Mr. Schwartz

CHAIRMAN OF THE BOARD OF GOVERNORS
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

Mr Southard

February 18, 1972.

Mr. Pierre-Paul Schweitzer,
Managing Director,
International Monetary Fund,
Washington, D. C., 20431.

Dear Pierre-Paul:

Thank you for your note of February 10 and the copies of the papers prepared by your staff dealing with reform of the international monetary system. These questions concern me greatly, and my staff and I will continue to give them our close attention.

Sincerely yours,

Arthur F. Burns

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

OFFICE OF THE VICE CHAIRMAN

December 27, 1971

Dear Pierre-Paul:

It was a real pleasure to receive your Holiday Greetings, and I hasten to say many thanks and extend warmest wishes to you and yours for a Good 1972.

Cordially,

J. L. Robertson

The Honorable Pierre-Paul Schweitzer
Managing Director
International Monetary Fund
1850 H Street, N. W.
Washington, D. C. 20431

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

Nov. 18, 1971

Dear Pierre-Paul,

I was deeply moved by your letter about the Rockefeller Award. We all enjoy praise, but I can think of no one whose praise I value more than yours.

I shall not be so presumptuous as to try to reciprocate your kind words about me. Let me say, though, that I have the greatest admiration for all that you have done, and continue to do, as President of what I regard as the emerging world central bank.

Most sincerely yours,
Bob

CHAIRMAN OF THE BOARD OF GOVERNORS
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

August 12, 1971

Dear Mr. Schweitzer:

You may be interested in the enclosed press release regarding a change in the size of the Federal Reserve swap arrangements with the National Bank of Belgium and the Swiss National Bank.

Sincerely yours,

Arthur F. Burns

The Honorable Pierre-Paul Schweitzer
Managing Director
International Monetary Fund
Washington, D.C.

Enclosure

FEDERAL RESERVE
press release

For immediate release August 12, 1971

The Federal Reserve announced today an increase in its reciprocal currency ("swap") arrangements with the Swiss National Bank and the National Bank of Belgium.

The arrangement with the Swiss National Bank has been increased by $400 million to $1 billion, and that with the National Bank of Belgium has been increased by $100 million to $600 million.

The increases enlarge the System's swap network with 14 central banks and the Bank for International Settlements to $11.73 billion.

A swap arrangement is a renewable short-term facility under which a central bank agrees to exchange on request its own currency for the currency of the other party up to a maximum amount over a limited period of time.

The Federal Reserve swap network was initiated in 1962. In all reciprocal currency arrangements the Federal Reserve Bank of New York acts on behalf of the Federal Reserve System under the direction of the Federal Open Market Committee. The Federal Reserve's reciprocal currency arrangements are now as follows (in millions of dollars):

Austrian National Bank	$ 200
National Bank of Belgium	600
Bank of Canada	1,000
National Bank of Denmark	200
Bank of England	2,000
Bank of France	1,000
German Federal Bank	1,000
Bank of Italy	1,250
Bank of Japan	1,000
Bank of Mexico	130
Netherlands Bank	300
Bank of Norway	200
Bank of Sweden	250
Swiss National Bank	1,000
Bank for International Settlements	
Swiss francs/dollars	600
Other European currencies/dollars	1,000
Total	$11,730

(Note: The foregoing announcement is also being released by the Federal Reserve Bank of New York)

Office Memorandum

TO : The Managing Director
The Deputy Managing Director

DATE: August 12, 1971

FROM : W.O. Habermeier WOH

SUBJECT : U.S. - Swap Facility

The Federal Reserve has just announced that their reciprocal credit facility (swap) with the National Bank of Switzerland has been increased from $600 million to $1 billion and that with the National Bank of Belgium has been raised from $500 million to $600 million. The total swap facilities of the Federal Reserve now amounts to $11,730 million. I attach a Table on the size of individual arrangements.

att.

Federal Reserve Reciprocal Currency Arrangements

(In millions of dollars)

Institution	Amount of facility
Austrian National Bank	200
National Bank of Belgium	600
Bank of Canada	1,000
National Bank of Denmark	200
Bank of England	2,000
Bank of France	1,000
German Federal Bank	1,000
Bank of Italy	1,250
Bank of Japan	1,000
Bank of Mexico	130
Netherlands Bank	300
Bank of Norway	200
Bank of Sweden	250
Swiss National Bank	1,000
Bank for International Settlements:	
Swiss francs-dollars	600
Other authorized European currencies-dollars	1.000
Total	11,730

As of August 12, 1971

October 6, 1970

Dear Arthur:

Your note to Mr. Schweitzer has reached his desk during his absence on a trip to a number of our Asian members which will keep him away from Washington until November 4. I am sure that he will want to take advantage of your suggestion of a get-together and I will see to it that your note comes to his attention as soon as he returns.

I very much enjoyed having the pleasure of being seated next to Mrs. Burns at the dinner in Copenhagen.

With best wishes, I am

Cordially yours,

Frank A. Southard, Jr.

The Honorable Arthur F. Burns
Chairman of the Board of Governors
of the Federal Reserve System
Washington, D. C. 20551

CHAIRMAN OF THE BOARD OF GOVERNORS
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

October 2, 1970

Dear Mr. Schweitzer:

Mrs. Burns and I would like to express our thanks for the pleasant dinner party that you and Mr. McNamara offered in Copenhagen.

I enjoyed our brief talk and I hope that we shall have an opportunity to get together soon and pursue further several subjects of mutual interest.

Sincerely yours,

Arthur F. Burns

The Honorable Pierre-Paul Schweitzer
Managing Director and Chairman
Board of Executive Directors
International Monetary Fund
Washington, D. C.

A STATEMENT OF THE TREASURY ON THE BRITISH BANK RATE.

The U.S. respects and understands the decision of the Bank of England to raise its bank rate to 7% in order to overcome the recent heavy pressures on sterling. The series of measures that have now been taken by the United Kingdom demonstrate the determination and ability of the British Government successfully to maintain the integrity of sterling.

DILLON'S STATEMENT ON FEDERAL RESERVE DISCOUNT RATE.

The Secretary of the Treasury Douglas Dillon this afternoon released the following statement:

The Federal Reserve has acted today to maintain the strength of the dollar without impairing the steady and healthy advance of the American economy.

Increasing the discount rate to 4% will make itpossible to maintain short term money rates in an appropriate alignment with those abroad. Recently there have been a number of increases in foreign official rates which culminated in today's increase in the Bank of England rate to 7%. The ceiling on rates payable for time deposits has also been raised to $4\frac{1}{2}$% to permit active competition by American banks for funds that might move internationally.

These moves together with cooperative action in the foreign exchange markets will avert an outflow of interest-sensivivenliquid funds from the United States and provide a base for further progress in strengthening our balance of payments flow position. At the same time the supply of sa ings and the ready availability of credit at reasonable rates within the United States which will not be diminished by these actions gives assurance that financing facilities will remain ample to support the continued expansion of our prospering eoconomy.

2

JUN 23 1964

Dear Bill:

I have your letter of June 22 telling us that the Presidents of all of the Federal Reserve Banks have expressed a desire to cooperate in our program of technical assistance in the field of central banking. We are particularly grateful for the generous list of names and biographies of very senior officials of the System who might be available from time to time. I also note that later you may be sending us the names of staff members of the Board of Governors.

The Central Banking Advisory Service is coming along very well. We have been able to supply several central bank officials from member countries to be temporarily assigned as officials in new central banks in other countries, and we feel that there will be a steady demand for this service over the years.

With cordial personal greetings, I am,

Sincerely yours,

S-

Pierre-Paul Schweitzer
Managing Director

Mr. Wm. McC. Martin, Jr.
Chairman of the Board
of Governors
Federal Reserve System
Washington, D. C.

cc: Mr. Clark

FASouthard:brs

June 23, 1964

April 1, 1964

Dear Bill:

Thank you very much for sending me a copy of the 50th Annual Report of the Board of Governors of the Federal Reserve System, which I am glad to have both to read and to refer to.

I understand we shall be meeting in Minneapolis towards the end of this month. I shall look forward to seeing you then, if our paths do not cross earlier.

With all good wishes,

Yours sincerely,

P.-P. Schweitzer
Managing Director

Wm. McC. Martin, Jr.
Office of the Chairman
Board of Governors of the
Federal Reserve System
Constitution Avenue
between 20th and 21st N.W.
Washington, D.C.

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Mr Southard
Mr Thomson
Kach ?

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

OFFICE OF THE CHAIRMAN

February 12, 1964.

Mr. Pierre-Paul Schweitzer,
Managing Director and Chairman of the
Board of Executive Directors,
International Monetary Fund,
19th and H Streets, N. W.,
Washington, D. C. 20431

Dear Pierre-Paul:

With further reference to Governor Balderston's letter to Mr. Southard dated August 16, 1963, the Board has endorsed, in principle, Federal Reserve cooperation in the program of the International Monetary Fund for providing technical assistance in the field of central banking.

The Presidents of the Federal Reserve Banks are being informed of the Board's action in this matter, and, if their individual Banks desire to participate, are being asked to nominate one or more persons for inclusion in the panel of experts that the Fund would like to establish.

Upon receipt of the replies from the Presidents of the Federal Reserve Banks, we will communicate with you again and supply a list of any persons either from the Banks or from the Board's staff whose names we feel might be included in the panel. It would be understood that, if the Fund should become interested in obtaining the services of any person whose name was included on the list, such a request would initially be presented to the Board by the Fund, and no direct approach would be made by the Fund to the individual until after the Board had considered the matter.

Sincerely yours,

Bill

Wm. McC. Martin, Jr.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

C. CANBY BALDERSTON
MEMBER OF THE BOARD

January 13, 1964.

Dear Mr. Schweitzer:

It is always a treat to hear from you and especially to see you here in the Building. I wish you the very best of health and satisfaction during the year ahead.

Have you ever seen such optimism?

With best regards,

Sincerely,

Canby Balderston

Mr. Pierre-Paul Schweitzer,
Managing Director,
International Monetary Fund,
19th and H Streets, N. W.,
Washington, D. C.

P.S. Your card came while Mrs. Balderston and I were on a belated "summer" holiday to Venezuela and points between.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

OFFICE OF THE CHAIRMAN

March 31, 1964.

The Honorable Pierre-Paul Schweitzer,
Chairman of the Board and
Managing Director,
International Monetary Fund,
19th and H Streets, N. W.,
Washington, D. C. 20431

Dear Pierre-Paul:

I am enclosing a copy of the 50th Annual Report of the Board of Governors, covering 1963, in the thought that it may be of use to you for reading or reference.

With all good wishes.

Sincerely yours,

Bill

Wm. McC. Martin, Jr.

Enclosure.

February 3, 1964

Dear Bill:

It was most thoughtful of you to send me a copy of The Federal Reserve System: Purposes and Functions. It looks to be a fund of information and I will be keeping it handy. Thank you so much.

Yours sincerely,

P.-P. Schweitzer

Mr. William McC. Martin, Jr.
Chairman of the Board
Federal Reserve System
Washington, 25, D.C.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

OFFICE OF THE CHAIRMAN

January 31, 1964.

The Honorable Pierre-Paul Schweitzer,
Chairman of the Board and Managing Director,
International Monetary Fund,
Washington, D. C. 20431

Dear Pierre-Paul:

We have just received initial copies of the fifth edition of The Federal Reserve System: Purposes and Functions, and I am enclosing a copy in the thought that you might find it useful for reading or reference. Directed like its predecessors to fostering understanding of the Federal Reserve and its operations, the new edition has been revised to bring the contents up to date and expanded to include chapters on the organization of the System for policy making, on the open market policy process, and on the balance of payments.

Sincerely yours,

Bill

Wm. McC. Martin, Jr.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

OFFICE OF THE CHAIRMAN

December 6, 1963.

Dear Pierre-Paul:

Just a line to thank you for coming over to the luncheon meeting of our Conference of Chairmen and Deputy Chairmen to explain the purposes and functions of the Monetary Fund and the problem of liquidity in the future so expertly and convincingly. I know that everyone benefited from it.

With all good wishes to you and Tochette,

Cordially yours,

Bill

Wm. McC. Martin, Jr.

The Honorable Pierre-Paul Schweitzer,
Managing Director,
International Monetary Fund,
Washington, D. C. 20431

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

December 5, 1963.

Dear Mr. Schweitzer:

I do not want to leave Washington without adding a word of thanks to you for speaking to the Reserve Bank Chairmen and Deputy Chairmen today. All of us appreciated the chance to hear your clear presentation of the origin and work of the Fund, and of some of the current problems you are dealing with.

Sincerely yours,

F. B. Whitman

F. B. Whitman, Chairman,
Conference of Chairmen.

The Honorable Pierre-Paul Schweitzer,
Managing Director,
International Monetary Fund,
Washington, D. C.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

OFFICE OF THE CHAIRMAN

November 18, 1963.

The Honorable Pierre-Paul Schweitzer,
Chairman and Managing Director,
International Monetary Fund,
Washington, D. C. 20431

Dear Pierre:

I am delighted that you will be able to talk informally and off the record to the Chairmen and Deputy Chairmen of the Federal Reserve Banks at lunch on December 5. If you will come to my office shortly before one o'clock we can go to the dining room together.

I am sending along a copy of the list of Chairmen and Deputy Chairmen who will be attending the luncheon, along with the Board Members and a few of the Board's staff.

Sincerely yours,

Bill

Wm. McC. Martin, Jr.

Enclosure

December 1963

CHAIRMEN AND FEDERAL RESERVE AGENTS, AND DEPUTY CHAIRMEN OF FEDERAL RESERVE BANKS

Bank	Chairmen and Federal Reserve Agents	Deputy Chairmen
Boston	Erwin D. Canham Editor The Christian Science Monitor One Norway Street Boston 15, Massachusetts	William Webster President New England Electric System 441 Stuart Street Boston 16, Massachusetts
New York	Philip D. Reed Formerly Chairman of the Board, General Electric Company. Mailing Address: Room 2709 375 Park Avenue New York 22, New York	James DeCamp Wise Formerly Chairman of the Board, Bigelow-Sanford, Inc. Mailing Address: R. D. #1 Frenchtown, N. J.
Philadelphia	Walter E. Hoadley Vice President and Treasurer Armstrong Cork Company Lancaster, Pennsylvania	David C. Bevan Vice President, Finance The Pennsylvania Railroad Company 6 Penn Center Plaza Philadelphia 4, Pennsylvania
Cleveland	Joseph B. Hall Chairman of the Board The Kroger Co. P. O. Box 1199 Cincinnati 1, Ohio	Logan T. Johnston President Armco Steel Corporation Middletown, Ohio
Richmond	Edwin Hyde President Miller & Rhoads, Inc. Richmond, Va.	William H. Grier President Rock Hill Printing & Finishing Company Rock Hill, South Carolina
Atlanta	Jack Tarver President Atlanta Newspapers, Inc. Atlanta 2, Georgia	Henry G. Chalkley, Jr. President The Sweet Lake Land & Oil Company Lake Charles, Louisiana

CHAIRMEN AND FEDERAL RESERVE AGENTS, AND DEPUTY CHAIRMEN OF FEDERAL RESERVE BANKS

Bank	Chairmen and Federal Reserve Agents	Deputy Chairmen
Chicago	Robert P. Briggs Executive Vice President Consumers Power Company Jackson, Michigan	James H. Hilton President Iowa State University of Science and Technology Ames, Iowa
St. Louis	Raymond Rebsamen Chairman of the Board Rebsamen & East, Inc. Tower Building Little Rock, Arkansas	J. H. Longwell Director Special Studies and Programs College of Agriculture University of Missouri Columbia, Missouri
Minneapolis	Atherton Bean President International Milling Company 1200 Investors Bldg. Minneapolis 2, Minnesota	Judson Bemis President Bemis Bro. Bag Co. 608 Second Avenue South Minneapolis 2, Minnesota
Kansas City	Homer A. Scott Vice President and District Manager Peter Kiewit Sons' Company Sheridan, Wyoming	Dolph Simons Editor and President The Lawrence Daily Journal-World Lawrence, Kansas
Dallas	Robert O. Anderson, Owner Lincoln County Livestock Co. Roswell, New Mexico ADDRESS ALL COMMUNICATIONS TO: Robert O. Anderson, Chairman Federal Reserve Bank of Dallas Station K, Dallas, Texas 75222	
San Francisco	F. B. Whitman President The Western Pacific Railroad Company 526 Mission Street San Francisco 5, California	John D. Fredericks President Pacific Clay Products 1255 West Fourth Street Los Angeles 17, California

Copies to
Mr. Southard +
Mr. Polak

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

OFFICE OF THE VICE CHAIRMAN

October 31, 1963.

The Honorable Pierre-Paul Schweitzer,
Managing Director,
International Monetary Fund,
Washington, D. C.

Dear Mr. Schweitzer:

You may be interested in the attached release concerning a new foreign currency arrangement between the Federal Open Market Committee and the Bank of Japan.

This will be given to the press at approximately 3:15 p.m. this afternoon (Thursday) by the Federal Reserve Bank of New York and will be released simultaneously here in Washington.

Sincerely yours,

C Canby Balderston

C. Canby Balderston,
Vice Chairman.

Enclosure.

FEDERAL RESERVE
press release

For immediate release. October 31, 1963.

FOR RELEASE 3:15 p.m., Thursday, October 31, 1963.

The Federal Reserve Bank of New York announced today that a reciprocal currency arrangement has been concluded with the Bank of Japan, on a standby basis, in the amount of $150 million (about 54 billion Japanese yen).

The new agreement brings the total of Federal Reserve reciprocal currency arrangements to $1.950 billion. These swap arrangements do not, in themselves, constitute outstanding liabilities, but, like the new Japanese arrangement, represent reciprocal facilities on a standby basis that may be drawn upon by either party from time to time.

In all such arrangements the Federal Reserve Bank of New York acts on behalf of the 12 Federal Reserve Banks under the direction of the Federal Open Market Committee.

The Federal Reserve now has reciprocal currency arrangements with the following banks:

	(In millions of dollars)
Austrian National Bank	50
National Bank of Belgium	50
Bank of Canada	250
Bank of England	500
Bank of France	100
German Federal Bank	250
Bank of Italy	250
Bank of Japan	150
Netherlands Bank	100
Bank of Sweden	50
Swiss National Bank	100
Bank for International Settlements	100

(Note: The foregoing announcement has also been issued by the Federal Reserve Bank of New York.)

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

OFFICE OF THE CHAIRMAN

October 10, 1963.

The Honorable Pierre-Paul Schweitzer,
Managing Director,
International Monetary Fund,
Washington, D. C.

Dear Pierre:

You may be interested in the attached release concerning foreign currency arrangements between the Federal Open Market Committee and other central banks.

This will be given to the press at approximately 3:15 p.m. this afternoon (Thursday) by the Federal Reserve Bank of New York and will be released simultaneously here in Washington.

Sincerely yours,

Bill

Wm. McC. Martin, Jr.

Enclosure.

FEDERAL RESERVE

press release

For immediate release. October 10, 1963.

NOTE: To be released to press at approximately 3:15 p.m., EDT, Thursday, October 10.

The Federal Reserve Bank of New York announced today that the reciprocal currency arrangements with the German Federal Bank and the Bank of Italy had both been increased from \$150 million to \$250 million (from 600 million to 1 billion German marks and from about 93.8 billion to about 156.3 billion Italian lire) and that the arrangement with the Netherlands Bank had been increased from \$50 million to \$100 million (from about 180 million to about 360 million Netherlands guilders). The Federal Reserve now has reciprocal currency arrangements totaling \$1.8 billion with the following banks:

	(In millions of dollars)
Austrian National Bank	50
National Bank of Belgium	50
Bank of Canada	250
Bank of England	500
Bank of France	100
German Federal Bank	250
Bank of Italy	250
Netherlands Bank	100
Bank of Sweden	50
Swiss National Bank	100
Bank for International Settlements	100

In all such arrangements the Federal Reserve Bank of New York acts on behalf of the 12 Federal Reserve Banks under the direction of the Federal Open Market Committee.

(Note: The foregoing announcement has also been issued by the Federal Reserve Bank of New York.)