

EMPLOYMENT, GROWTH, AND PRICE LEVELS

HEARINGS

BEFORE THE

JOINT ECONOMIC COMMITTEE

CONGRESS OF THE UNITED STATES

EIGHTY-SIXTH CONGRESS

FIRST SESSION

PURSUANT TO

S. Con. Res. 13

JULY 24, 27, 28, 29, AND 30, 1959

PART 6A—THE GOVERNMENT'S MANAGEMENT OF ITS
MONETARY, FISCAL, AND DEBT OPERATIONS

Printed for the use of the Joint Economic Committee

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STUDY OF EMPLOYMENT, GROWTH, AND PRICE LEVELS

(Pursuant to S. Con. Res. 13, 86th Cong., 1st sess.)

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EMPLOYMENT, GROWTH, AND PRICE LEVELS

FRIDAY, JULY 24, 1959

CONGRESS OF THE UNITED STATES,
JOINT ECONOMIC COMMITTEE,
Washington, D.C.

The committee met at 10 a.m., pursuant to notice, in the Old Supreme Court Chamber, the Capitol, Senator Paul H. Douglas (chairman of the committee) presiding.

Present: Senators Douglas, Bush, and Javits; Representatives Curtis, Widnall, Patman, Reuss, and Coffin.

The CHAIRMAN. Gentlemen, the committee will come to order.

We begin this morning with perhaps the most important series of hearings this committee will conduct on the problems of money supply and debt management in relationship to economic conditions.

We greatly appreciate the courtesy of the Secretary of the Treasury, Mr. Anderson, is taking time from a busy life to appear before us.

We may not always agree with the Secretary, but we have great respect for him as a devoted public servant. I will say openly what I have frequently told him privately, that he is, I think, the most courteous Government official whom I have ever seen appear before a congressional committee.

Mr. Anderson, I understand that you and Chairman Martin have agreed on a joint statement relative to the study which you have conducted on the Government securities market, which was distributed to the members of the committee yesterday, and that this is to be made a part of the record, not read but subject to discussion, but that you would like to submit orally a briefer statement more general in character which you think you could do in 20 minutes or so.

Mr. ANDERSON. Yes, sir.

The CHAIRMAN. We will be very glad to hear you, and at the end of that time we will have some questions from members of the committee.

STATEMENT OF HON. ROBERT B. ANDERSON, SECRETARY OF THE TREASURY; ACCOMPANIED BY JULIAN B. BAIRD, UNDER SECRETARY OF THE TREASURY FOR MONETARY AFFAIRS; CHARLES E. WALKER, ASSISTANT TO THE SECRETARY; ROBERT P. MAYO, ASSISTANT TO THE SECRETARY; NILS LENNARTSON, ASSISTANT TO THE SECRETARY; AND R. DUANE SAUNDERS, CHIEF, DEBT ANALYSIS STAFF, DEPARTMENT OF THE TREASURY

Secretary ANDERSON. Mr. Chairman, may I first express my appreciation for the opportunity afforded us to appear before this com-

mittee, and say that I always find the appearances before committees in which the distinguished chairman participates of great value to us in our own thinking.

Our national economic objectives can be summarized under three broad headings: (1) continuity of employment opportunities for those able, willing, and seeking to work; (2) a high and sustainable rate of economic growth; and (3) reasonable stability of price levels. Each of these objectives is important; each is related to the others.

The rapid upsurge in economic activity of the past 15 months provides an appropriate background for your study of these national economic goals and the best methods of achieving them. The recent resurgence in output, income, and employment to record levels has once again demonstrated the basic strength and resilience of our free choice, competitive economy. Thus, we visualize the task with which your committee is confronted not as one of devising drastic changes in our techniques for achieving our economic goals. Rather, it is to evaluate, within the perspective of developments of the past few years and during the postwar period as a whole, the existing techniques toward the end of sharpening their use. There may perhaps be weapons not now in our arsenal that should be developed. There are, no doubt, ways in which existing techniques can be improved. But the performance of our economy supports the judgment that basically our economy is sound and healthy.

Much could be said about government economic techniques, their nature, interrelationships, strengths, and shortcomings. I am sure, however, that your committee will explore these matters thoroughly, drawing both from current thinking and from the vast body of earlier study performed both by committees of the Congress and by private individuals and organizations.

Before discussing the Treasury-Federal Reserve study of the Government securities market, in which you have expressed particular interest, I should like to consider briefly economic growth as a goal of public policy.

Some in our country express a belief that the Government should undertake the primary role in promoting economic growth. It is my belief that in our system the Government is not the predominant factor in our Nation's economic advancement. It must foster and facilitate economic progress; it cannot force it.

What we all seek is sound substantial growth, not any kind of growth, or growth at any cost.

Should our efforts to spur progress lead to inflation it will bring only disappointment and hardship. But when growth is in terms of goods and services that people need and can buy, it will bring great rewards.

Only within the past decade has economic growth been explicitly recognized as a major goal of public policy. This recognition, coupled with considerable public discussion of the importance of growth to our economy, provides an important reason for taking a careful look at growth as a national economic objective.

What is economic growth? What determines the rate of economic growth in a free-choice market economy? And, finally, what is the proper role of government in promoting a high and sustainable rate of economic growth?

What is economic growth? The most commonly cited definition of economic growth is in terms of the annual advance in real gross national product; that is, growth in the dollar value of total output, adjusted for changes in price levels. For some purposes this is a good measure of economic growth; for others it is not.

An overall measure of growth tells us nothing about its nature. For any period, we must get behind the broad figures to determine what type of growth has taken place. This is simply another way of saying that promotion of growth for its own sake may well result in either fictitious or unsustainable growth. An increase in output, to be meaningful, must consist of the goods and services that people want and are able to buy. It is not enough to select some hypothetical maximum of growth. The actual growth that occurs must consist of useful and desirable things as opposed to unwanted or undesirable goods.

Thus, in trying to decide whether growth over a period of years was at an adequate rate, we would first have to look within the total, to get behind the figures, and try to determine the characteristics of the growth.

Some of the questions we would ask would be:

How much did personal consumption expand relative to Government use of goods and services? Within the Government component, what portion consisted of defense spending as opposed to schools, highways, and other public facilities?

How much of the increase in output consisted of goods the people did not want, and thus ended up in Government warehouses, being given away or destroyed?

What portion of total output was devoted to investment in the instruments of production, to modernization of plant and equipment, and to research?

How much of our effort had to be devoted merely to maintenance of our productive plant, as opposed to net new additions?

There are other important questions.

How were the fruits of the growth in output distributed among various groups in the economy?

Did the growth carry with it certain imbalances that would hamper future growth?

To what extent was temporary growth fostered by reliance on actions that impinged directly on the free choice of individuals and institutions?

These are but a few of the questions we should ask. They indicate that economic growth, in terms of a broad, aggregate figure, is not necessarily an end in itself. It must be growth of the right kind; it must be sustainable growth.

What determines the rate of economic growth? The role of public policy in fostering a high and sustainable rate of economic growth in a free-choice, competitive economy can be properly assessed only on the basis of an understanding of the determinants of growth.

The factors influencing the rate of growth are manifold and complex. Among those of major importance is the pace of technological advance. No one can study the economic history of this or any other advanced industrial nation without being impressed by the vital contributions of the inventor, the innovator, and the engineer. A stagnant technology is likely to be accompanied by a stagnant econ-

omy. Man's ingenuity in tackling and solving his problems lies at the heart of the growth process.

This is perhaps another way of saying that growth and change are inseparably intertwined. If we would enjoy maximum growth, we must not only be willing to improve the production process through accepting new ways of doing things, but we must also actively seek out such techniques. Moreover, the integral role played by change and technological advance in the growth process contributes to unevenness in growth over time. Technological advance does not come at a steady, constant rate. Thus we cannot expect growth, to the extent it reflects such forces, to proceed at a steady rate year in and year out.

Technological advance, however, cannot alone assure a high rate of growth. The best ideas and the best techniques are of little benefit if the means are not available to translate them into operating productive processes. This requires real capital, which can only grow out of saving and productive investment. Thus, real capital formation—which consists of the machinery and instruments of production, tools of all sorts, and new plant buildings—is a basic ingredient of economic growth. An economy in which additions to the stock of capital equipment are small cannot be a rapidly growing economy.

The importance of an adequate rate of capital formation in the growth process deserves special emphasis. Broadly speaking, current output can be directed either into consumption goods, represented by durable and nondurable consumer goods and services, or into investment goods, represented principally by new industrial plant and equipment. So long as our economic resources are being utilized close to capacity, as has indeed been the case almost continuously since 1941, the more of our output we devote to capital formation, the less that is available for current consumption. The more we consume, the less we can devote to capital formation.

This is a basic but apparently little understood principle of economics. There appear to be some observers who believe that, on top of providing adequately for national defense and devoting a considerably larger volume of current output to public projects, we can still achieve uninterrupted future growth in the private sector of the economy at a rate higher than ever before realized in this country. Perhaps this is possible, but it seems clear to me that it can occur only at the expense of current consumption. It can take place, in other words, only if we are willing to accept a lower current standard of living. With our pressing needs for adequate national defense, we cannot have an ultrahigh "maximum" rate of economic growth in the future, requiring as it does heavy current investment in plant and equipment, without restricting current consumption. We cannot have our cake and eat it, too.

A third important requisite for a high and sustained rate of growth is reasonably full, efficient, and continuous use of our economic resources. Economic recession is the No. 1 enemy of sustained growth in this country. Idle manpower and idle equipment represent production that is irretrievably lost. Moreover, inefficiencies in use of resources can also carry a heavy toll in terms of lost output.

It is important to emphasize that success in achieving high and sustained employment, and in providing useful job opportunities for our

growing population is closely related to our success in promoting an adequate rate of capital formation. In our highly industrialized economy, workers must have the machines with which to work. These machines will come into existence only to the extent that productive investment takes place.

In short, economic growth in a free-choice, competitive economy tends to vary more or less directly with the pace of technological advance, the rate of capital formation and the extent to which economic resources are effectively employed. To be effective, any government program designed to foster growth must operate largely through these basic determinants.

Government's role in fostering growth: Government can play an important role in fostering a high and sustainable rate of economic growth. One basic principle should be clear, however. In an economy in which major reliance is placed on individual initiative and decisions and in which the alternative uses of economic resources respond through the market mechanism, primarily to consumer demand, government can and should play only a facilitating, not a predominant, role in the growth process.

The moving forces which promote growth in a free-choice market economy are basically the same as those that account for economic progress on the part of the individual. Thus, the individual's desire for a higher and more secure standard of living for himself and for his family is the basic stimulus. This is the prime mover: To this end he studies, plans, works, saves, and invests. He searches out new ways of doing things, developing new techniques and processes. Where such instincts as these are strong, the forces promoting growth in society as a whole are strong. Where they are weak, the impetus for growth is also weak.

The first role of Government in promoting growth is to safeguard and strengthen the traditions of freedom in our economy. Stated differently, the proper and effective role of Government is to provide an atmosphere conducive to growth, not directly to attempt to force growth through direct intervention in markets or through an imprudent enlargement of the public sector of the economy. Indeed, governmental efforts to promote growth that rely on, or subsequently lead to, excessive intervention in and direction of market processes can only impede growth in the long run.

The case for this approach to promoting growth is strengthened by the fact that technological advance flourishes in an atmosphere of freedom. Basic to technological advance is pure research, and a fundamental belief in our society that pure research makes its greatest contribution when minds are free to meet the challenges of the future.

Government can also promote rapid, healthy growth by fostering competition in the economy. Competition sharpens interest in reducing costs and in developing more efficient methods of production. It places a premium on skills in business management. It stimulates business investment, both as a means of economizing in the production process by use of more efficient machinery and by enlarging capacity in order to capture a larger share of the market. Healthy and widespread competition, in short, is the primary stimulant to efficiency in use of our economic resources, both human and material,

through technological advance and by stamping out waste and inefficiency in productive processes.

Our tax system may hamper growth in a number of ways. One of the objectives of the study recently initiated by the House Ways and Means Committee, and in which the Treasury is cooperating, is to determine what changes can be made that will be conducive to healthy and sustainable economic growth. I am hopeful that this study will lead to significant results.

All of these methods of aiding growth are important. I am convinced, however, that Government can make a most significant contribution to growth primarily by using its broad financial powers—fiscal, debt management, and monetary policies—to promote reasonable stability of price levels and relatively complete and continuous use of our economic resources.

As noted earlier, a high rate of saving is indispensable in achieving a high rate of economic growth. Under conditions of near-capacity production, resources can be devoted to capital formation only to the extent that they are freed from output of goods for current consumption. This, in turn, is possible only to the extent that saving occurs.

In the years since the war, incentives to save in traditional forms—in savings accounts, bonds, and through purchasing insurance—have been somewhat impaired by the conviction of some that inflation is inevitable. In my judgment, this is a mistaken conviction. But the fact remains that if we allow a lack of confidence to develop in the future value of the dollar, the desire to save will be weakened.

Full confidence in the future value of the dollar can be maintained and strengthened only by a concerted, broad-gauge attack on all of the forces and practices that tend to promote inflation. Some of these forces and practices may be new and thus require further study before they can be identified and before appropriate policies to control them can be devised. But there should be little doubt in our minds as to the proper role of general stabilization policies. Under present-day conditions, with production, employment, and income advancing rapidly to record levels, such policies should be directed toward self-discipline and restraint. This requires Federal revenues in excess of expenditures to provide a surplus for debt retirement, flexible management of the public debt, and monetary policies directed toward preventing excessive credit expansion from adding unduly to overall demand for goods and services.

Some observers have argued recently that we are not now confronted with monetary inflation or with a situation in which "too much money is chasing too few goods."

The CHAIRMAN. Mr. Anderson, lest there be any doubt to whom you are referring, may I identify myself as one of those who made this comment.

Secretary ANDERSON. Thank you, sir.

They point to the high degree of price stability during the past year as proof of this contention.

This same argument could well have been made in mid-1955, when that recovery was also merging into the boom phase of the cycle. At that time the Consumer Price Index had actually declined slightly during the preceding 18 months; the wholesale price index had been stable for about 30 months.

We failed to recognize at that time, just as we may be in danger of failing to recognize now, that the high levels of demand generated in the recovery had sown the seeds of later increases in prices. Thus, wholesale prices rose moderately in the last half of 1955, at a steady and relatively rapid rate throughout 1956, and moderately during 1957. Consumer prices, exhibiting the customary lag, did not begin to advance until the spring of 1956, but thereafter rose steadily until early 1958.

The important point is that effective control of inflation requires actions to restrain inflationary pressures at the time that such pressures are developing. To wait until the pressures have permeated the economy and have finally emerged in the form of price increases is to delay action until the situation is much more difficult to cope with.

Effective stabilization actions to limit inflationary pressures during this period of rapid business expansion, in addition to promoting stability of price levels, will stimulate sustained growth in still another important way. Such policies, by helping to assure that the current healthy advance in business activity does not rise to an unsustainable rate and then fall back, would promote relatively full and continuous use of our economic resources. I am firmly convinced that the degree of severity of a business recession reflects to a considerable extent the development of unsustainable expansion in the preceding boom. By exercising restraint and moderation during periods of prosperous business we can keep booms from getting out of hand, and, in so doing, minimize the impact of later adjustments.

Appropriate current governmental policy to promote growth must be consistent with long-range objectives and not resort to quick expedients that endanger sustainable development. We must reject the arguments of those who would attempt to force growth through the artificial stimulants of heavy Government spending and excessive expansion of money and credit.

If we would foster growth—not of the temporary, unsustainable type, but long-lasting and rewarding—we need first to reinforce our efforts to maintain reasonable price stability and relatively full and continuous use of our economic resources.

Both logic and experience demonstrate clearly that heavy reliance on Government spending and monetary and credit excesses during a period of strong demand, rather than promoting growth, can lead only to inflation. Inflation tends to dry up the flow of savings and leads ultimately to recession, the No. 1 enemy of growth.

We live in what is basically a free-choice economy. Within rather broad limits we are free to dispose of our labor, property, and incomes as we see fit. In disposing of our incomes we are free to spend or to save, to invest or to hoard. So long as we maintain the basic freedoms that foster competitive enterprise and stimulate technological advance, and so long as we use our broad financial powers to promote stability in the value of our currency and to avoid the extremes of economic recession, I am confident that economic growth will proceed at a high and sustainable rate. The strength of our economy lies in its very reliance on the integrity, wisdom, and initiative of the individual. We must not weaken this basic strength.

The Government securities market study: I will now make some brief observations on the Treasury-Federal Reserve study of the Government securities market.

Our national economic objectives are, of course, fundamental. It is only in relation to the successful achievement of these objectives that the financial policies pursued by our Government can have real meaning. Furthermore, fiscal, debt management and monetary policies can make their maximum contribution to national economic goals only if they can operate in a market which is responsive to policy actions both in terms of basic understanding of those actions by the investing public and in terms of the efficiency and maximum usefulness of market organization.

The Government securities market is the largest financial market in the world, with a daily trading volume of more than \$1 billion. It is an extremely complex market and is sharply competitive. It is very responsive to trends and expectations as to business activity, Government policies and international developments.

Its responsiveness and competitiveness, under widely varying circumstances, mean that it can provide the proper environment for the successful flotation of the tremendous volume of frequent Treasury security offerings to the public, which last year alone totaled almost \$50 billion, exclusive of the rollover of weekly Treasury bill maturities. Similarly, it can provide an efficient mechanism through which Federal Reserve monetary policy can operate. Moreover, it must provide for the smooth transfer of large amounts of Government securities among investors as liquidity and investment needs are satisfied.

The Treasury, the Federal Reserve and the entire business and financial community, therefore, have a joint responsibility, collectively and individually, to encourage the market to resist any forces which threaten to impair its maximum performance. If market techniques become distorted or restrictive practices arise, the consequences can extend far beyond any immediate impact on investors, speculators or suppliers of credit. It can undermine the basic contribution which a smoothly functioning Government securities market should make to the national welfare.

It is with this realization of the importance of the Government securities market that the Treasury and Federal Reserve last spring undertook their joint study of the way in which the market operates, with particular reference to the market's performance around the time of the reversal of the economic downturn a little more than a year ago.

A study of market mechanisms is necessarily technical. The results of any such study are understandably less dramatic than studies of the broad aspects of fiscal, monetary and debt management policy which, together with general economic trends and expectations, provide the environment in which these market mechanisms operate.

Our joint Treasury-Federal Reserve study group has been working continuously toward the objectives which were laid out when the project was announced on March 9, 1959. Part I of the study group's factual report is now in final form; parts II and III are only in preliminary form. All three parts are being made available for public release on Monday morning.

The CHAIRMAN. Mr. Secretary, do I understand that members of the committee will be furnished with copies of these three volumes this afternoon?

Secretary ANDERSON. Yes, they will, as soon as they are delivered to us.

The CHAIRMAN. Thank you.

Secretary ANDERSON. Your committee already has a joint statement by Chairman Martin and myself relating to the study. The virtual completion of the factual study by the study group provides a background which Federal Reserve and Treasury policy officials can now carefully review as we work toward official conclusions and recommendations growing out of the study.

These conclusions cannot be prejudged. Treasury and Federal Reserve officials have been following the progress of the study group with great interest, but, because of the late completion of the report, we have had little opportunity to examine the factual material which the study group has assembled.

As Chairman Martin and I state in the concluding paragraphs of our joint statement, markets are dynamic institutions which require adaptation to changing needs. The public interest is served only if the study of these adaptations is continuous, even though it may be intensified from time to time as in the present study.

We both recognize—and I want to emphasize it again—that improvements in market mechanisms, helpful though they may be, cannot be expected to solve the basic financial problems which our Nation faces—the problems of fiscal imbalance during prosperous times, the tendency for the public debt to grow shorter in its maturity structure, the need for continuous flexibility in adapting monetary policies to varying circumstances, the need to encourage increased savings to finance soundly the Nation's heavy capital requirements, and the problem of the instability of financial markets as they react to turning points in economic cycles.

These are basic problems. We are glad to work with your committee in seeking their solutions in the best interest of the public.

The CHAIRMAN. Thank you, Mr. Secretary.

I have read your very full statement to the House Ways and Means Committee which you gave some weeks ago. I understood from that that it is your contention that the Treasury, in its issues of public debt and refunding, does not make interest rates, but has to conform to competitively set interest rates determined by other groups in the general money market. Am I correct in that?

Secretary ANDERSON. Yes, sir.

The CHAIRMAN. And this carries out the very vivid illustration given by your predecessor, Mr. Humphrey, who likened the position of the Treasury in borrowing money on the money market to a housewife going in to buy a dozen eggs. Just as the housewife, so Mr. Humphrey said, had no influence on the price of eggs, so the Treasury could have no influence on the price of money.

I have not looked up the most recent figures on the production of eggs, but I think there are somewhere around a billion dozen eggs produced a year. Therefore, the housewife would have the effect of one-billionth upon the total market, and thereafter it would be infinitesimal.

I have, however, asked the staff to prepare figures on the relative amount of money borrowed by the Federal Government as compared with the total amount of money borrowed by State and local governments and corporations, and I have tables which I would like to have

placed in the record, which I think are substantially accurate, and the accuracy of which perhaps you can check as I give them.

Representative CURTIS. May I ask a question about the tables?

The CHAIRMAN. Yes.

Representative CURTIS. They do not include consumer credit?

The CHAIRMAN. That is true.

Representative CURTIS. Was there a reason for leaving that out?

The CHAIRMAN. No, I do not think there was any reason for leaving it out.

Representative CURTIS. Don't you think that is a very important factor?

The CHAIRMAN. Yes, I think it is important, and if the gentleman from Missouri will permit me to introduce this into the record, then perhaps qualifications can be made.

(The tables referred to follow:)

Federal Government issues of certificates, notes, and bonds: By purpose of issue, 1945-58

[Dollars in billions ¹]

Year	Total (1)	New capital (2)	Refunding (3)	Col. (2), col. (1) (percent) (4)	Col. (3), col. (1) (percent) (5)
1945	\$74.1	\$39.6	\$34.5	53.4	46.6
1946	30.0		30.0		100.0
1947	28.8		28.8		100.0
1948	30.1		30.1		100.0
1949	34.0		34.0		100.0
1950	38.1		38.1		100.0
1951	30.6		30.6		100.0
1952	33.7	4.2	29.5	12.5	87.5
1953	44.2	9.3	34.9	21.0	79.0
1954	59.7	10.1	49.6	16.9	83.1
1955	49.2	11.7	37.5	23.8	76.2
1956	33.6	3.2	30.4	9.5	90.5
1957	55.8	9.1	46.7	16.3	83.7
1958	62.2	11.3	50.9	18.2	81.8

¹ Source: Treasury Bulletins.

State and local governments' securities issues: By purpose of issue, 1945-58

[Dollars in billions ¹]

Year	Total (1)	New capital (2)	Refunding (3)	Col. (2), col. (1) (percent) (4)	Col. (3), col. (1) (percent) (5)
1945	\$0.8	\$0.5	\$0.3	62.5	37.5
1946	1.2	1.0	.2	83.4	16.7
1947	2.4	2.3	.1	95.8	4.2
1948	3.0	2.8	.2	93.3	6.7
1949	3.0	2.9	.1	96.6	3.4
1950	3.7	3.6	.1	97.3	2.7
1951	3.3	3.2	.1	97.0	3.0
1952	4.4	4.1	.3	93.2	6.8
1953	5.6	5.5	.1	98.2	1.8
1954	7.0	6.8	.2	97.1	2.9
1955	6.0	5.9	.1	98.3	1.7
1956	5.4	5.3	.1	98.1	1.9
1957	7.2	7.1	.1	98.6	1.4
1958	7.8	7.7	.1	98.7	1.3

¹ Sources: 1957-58, Investment Bankers Association; 1946-56, Bond Buyer. The two series are not directly comparable.

Total securities issues of the Federal Government, State and local governments, and corporations: By purpose of issue, 1945-58

[Dollars in billions]

Year	Total issues ¹	Total securities issues for new capital ²	Total securities issues for refunding	Col. (2) ÷ col. (1) (percent)	Col. (3) ÷ col. (1) (percent)
	(1)	(2)	(3)	(4)	(5)
1945.....	\$80.8	\$41.4	\$39.4	51.2	48.8
1946.....	38.0	4.9	33.1	12.9	87.1
1947.....	37.7	7.4	30.3	19.6	80.4
1948.....	40.1	9.5	30.6	23.7	76.3
1949.....	43.0	8.5	34.5	19.8	80.2
1950.....	48.1	8.6	39.5	17.9	82.1
1951.....	41.5	10.3	31.2	24.8	75.2
1952.....	47.5	17.0	30.5	35.8	64.2
1953.....	58.6	23.3	35.3	39.8	67.9
1954.....	76.1	24.4	51.7	32.1	60.2
1955.....	65.2	26.4	38.8	40.5	59.5
1956.....	49.7	18.9	30.9	38.0	62.0
1957.....	75.7	28.6	47.0	37.8	62.2
1958.....	81.4	29.8	51.6	36.6	63.4

¹ Securities issues of the Federal Government includes only certificates, notes, and bonds.

² The Federal Government component is new money.

*Corporations' securities issues: By purpose of issue, 1945-58**

[Dollars in billions]

Year	Total issues ¹	Total securities issues for new capital ²	Total securities issues for refunding	Col. (2) ÷ col. (1) (percent)	Col. (3) ÷ col. (1) (percent)
	(1)	(2) ³	(3) ³	(4)	(5)
1945.....	\$5.9	\$1.3	\$4.6	22.0	78.0
1946.....	6.8	3.9	2.9	57.4	42.6
1947.....	6.5	5.1	1.4	78.5	21.5
1948.....	7.0	6.7	.3	95.7	4.3
1949.....	6.0	5.6	.4	93.3	6.7
1950.....	6.3	5.0	1.3	79.4	20.6
1951.....	7.6	7.1	.5	93.4	6.6
1952.....	9.4	8.7	.7	92.6	7.4
1953.....	8.8	8.5	.3	96.6	3.4
1954.....	9.4	7.5	1.9	79.8	20.2
1955.....	10.0	8.8	1.2	88.0	12.0
1956.....	10.7	10.4	.4	96.3	3.7
1957.....	12.7	12.4	.2	98.3	1.6
1958.....	11.4	10.8	.6	94.7	5.3

¹ Securities issues of the Federal Government includes only certificates, notes, and bonds.

² The Federal Government component is new money.

³ Cols. (2) and (3) may not add to total because of rounding.

*Source: Securities and Exchange Commission.

Average maturity of the Federal marketable interest-bearing public debt: Semi-annually, December 1949 through December 1958¹

End of period	Average maturity		End of period	Average maturity	
	Years	Months		Years	Months
1949—December.....	8	9.0	1954—December.....	5	5.9
1950—June.....	8	2.5	1955—June.....	6	9.6
December.....	8	1.1	December.....	6	5.5
1951—June ²	6	6.8	1956—June.....	5	4.5
December.....	6	1.0	December.....	4	10.8
1952—June.....	5	8.4	1957—June.....	4	9.3
December.....	5	3.3	December.....	4	6.6
1953—June.....	6	3.8	1958—June.....	5	2.9
December.....	5	.2	December.....	4	9.3
1954—June.....	5	6.0			

¹ Source: Treasury Department. All issues classified by final maturity date, except partially tax-exempt bonds which are classified by earliest call date.

² On Apr. 1, 1951, the Treasury offered holders of a 2½-percent bond an exchange for 2¾-percent investment bonds, series B, maturing Apr. 1, 1980. The new securities were exchangeable for 1½-percent marketable notes, but were nonmarketable as such. Thus, the rather sharp drop in the average maturity of the debt over the first 6 months of 1951.

Total debt and Federal debt: Selected years, 1929–58

[In billions of dollars]

End of year	Total gross debt	Total gross Federal debt	Total gross Federal debt as percent of total gross debt
1929.....	\$214.4	\$16.3	7.60
1934.....	197.3	28.5	14.45
1939.....	207.7	41.9	20.17
1944.....	430.9	232.14	53.87
1945.....	463.3	278.7	60.15
1946.....	457.9	259.4	56.65
1947.....	485.6	257.0	52.92
1948.....	498.6	252.9	50.72
1949.....	520.3	257.2	49.43
1950.....	566.4	256.7	45.32
1951.....	607.5	259.5	42.72
1952.....	646.0	267.4	41.39
1953.....	683.6	275.2	40.26
1954.....	714.0	278.8	39.05
1955.....	786.2	280.8	35.72
1956.....	830.7	276.7	33.31
1957.....	865.1	275.0	31.79
1958.....	901.8	283.0	31.38

Sources: Total Gross Debt: Survey of Current Business, September 1953, May 1957, May 1959. Total Gross Federal Debt: Federal Reserve Bulletins.

The CHAIRMAN. If I may now proceed, this excludes bills. It does not include the 30-day and 60-day bills. It does include the issues of certificates, notes, and bonds. This excluded bills because that corresponded to commercial bank credits more closely, being of short duration.

These figures indicate that in 1958, the total Government issue was approximately \$62.2 billion, of which \$11.3 billion was for new money and \$50.9 billion consisted of refunding.

Are those figures approximately accurate?

Secretary ANDERSON. Yes, sir.

The CHAIRMAN. And similarly for State and local governments, the corresponding figure, \$7.8 billion, of which \$7.7 billion was for new capital and \$100 million refunding.

I do not know whether you have those figures. Are those approximately correct?

Secretary ANDERSON. Yes. I do not have them exactly.

The CHAIRMAN. The corporation securities total \$11.4 billion, of which \$10.8 billion was for new securities, and \$600 million refunding, making a total of these three forms of the money market of \$81.4 billion, of which the Government issues comprise 62.2 percent. In other words, instead of one-billionth of the total market, the Government borrowed three-quarters of the funds in the market, excluding consumer credit.

Are not the borrowings of the Government of such large volume, both actually and comparatively, that they help markedly to determine the interest rates instead of merely conforming to an interest rate fixed by other forces? That is the first question I wanted to ask.

Secretary ANDERSON. Senator Douglas, if I may first comment on your figures, perhaps I did not get all of them, but I did not hear a figure for mortgages in this compilation.

The CHAIRMAN. Real estate mortgages?

Secretary ANDERSON. Yes. You probably would want to include them.

I should also like to say this. We recognize that the Treasury is the biggest borrower in the country, and we recognize that we influence the cost of money.

The CHAIRMAN. And the interest rate.

Secretary ANDERSON. And the interest rate.

The CHAIRMAN. That is a very important point, because Mr. Humphrey has always denied this.

Representative CURTIS. Oh, no, no.

May I interpose an objection?

The CHAIRMAN. Surely.

Representative CURTIS. You are entitled to your interpretation, but I think you have always carried his statements to the extreme. He never said, in my judgment, that it did not influence it. Rather, he always minimized the influence in relation to what the gentleman from Illinois thought was the influence.

Secretary ANDERSON. I should like to say that as the biggest borrower we recognize the fact that we do influence the cost of money. We do not fix the cost of money. Although we are the biggest single borrower, we cannot control the supply of credit in a free market.

I think also that as we look at the Treasury operations in a year in the order of magnitude which you mentioned, we must also have an awareness that refundings, which comprise the largest part of our operations, do not have the same effect as going into the market for new cash, which is draining off current savings.

The CHAIRMAN. We have included the refundings of private corporations and of State and local governments, although, of course, proportionately they are much smaller in those cases.

Secretary ANDERSON. Yes. I simply wanted to make the point that in the order of magnitude there is a difference in the effect which we will have, if we refund it.

The CHAIRMAN. Now, if I may go into the analogy between the money market and other markets.

The economists say that where the supply is controlled by one party, you have complete monopoly, or where it is controlled by a few, you have highly imperfect competition between sellers.

When you have such a large proportion of borrowings made by one agency of Government, do we not have something departing very much from pure competition and approaching what the economists call monopsony—not complete monopsony, of course, but a type in which one buyer purchases the major portion of the supply?

Secretary ANDERSON. Senator Douglas, I think that in a very real sense it is doubtful if there is anything that is perfectly competitive. However, if we compare credit markets with other markets, the credit market seems to me to be one of the really competitive markets.

Also in the last 30 years this competition has grown.

How do we judge the degree of competitiveness in a market? One of the most important things is the alternatives that are open to the buyers and the sellers, or in credit markets the alternatives that are open to the lenders and to the borrowers.

Lenders are confronted with a variety of alternatives, both from the standpoint of the issuance of the obligations and from the standpoint of the maturity of the various securities. As a matter of fact one of the problems which we in the Treasury confront in issuing new issues of long-term Government securities is the fact that we face an increased competition for the lender's dollar.

I pointed out in my statement before the House Ways and Means Committee the variety of investments which are now available to people who do want to lend, particularly in the number of securities or mortgages that have grown in the last 8 or 10 years which carry some degree of guarantee, ranging all the way from a full guarantee by the U.S. Government simply to the fact that it has been issued by a Government agency and carries the implication that the Government would not permit a default.

Borrowers also have a number of alternatives. Let us take, for example, a man who wants to buy a house. If in the twenties he had wanted to buy a house he would have had to finance the transaction largely through a short-term mortgage note, which he hoped that he could repay or refinance at maturity. Today, he can borrow money from a commercial bank on that basis, or he can go to a savings bank, he can go to a building and loan association, he can go to an insurance company, he can go to a mortgage banker or, he can utilize some of the agencies of the Government, and most of these loans are amortized and paid off month by month.

You take consumers, such as the buyers of automobiles. There is high competition between whether those loans are held by the banks or by finance companies, small-loan companies, or even, in some instances, corporations created by the sellers of the goods, through which they can operate.

A businessman also has a variety of choices. He can shift from one place to the other.

Another thing you use to judge competitiveness is price behavior. If the prices in the market tend to remain fixed for a long period of time, or if the only type of movement is an irregular upward adjustment, then one would become concerned with the lack of competitiveness or monopolistic tendencies.

Certainly, prices in credit markets, and particularly the Government market, with which I am most immediately concerned, move very flexibly.

The CHAIRMAN. Mr. Anderson, our time will be up in a few minutes. I do want to raise this point, however, with just one more question.

If you, however, compare the money market now with the money market 30 years ago, then the national debt was only about \$20 billion, as I remember it, and now it is \$285 billion; the annual volume of borrowings, excluding bills as I have said, is \$62 billion; and the total Government debt is approximately one-third of the total debt in the country. If you compare this condition with the condition 30 years ago, certainly the Federal Government now is a much larger borrower, both absolutely and relatively, than it was then. Is that not true?

Secretary ANDERSON. That is correct, but even then the Government was the largest single borrower.

The CHAIRMAN. And while it might have been true 30 years ago that the Government had to conform to a competitively determined interest rate, is it not true now that it influences the interest rate much more than it did years ago?

Secretary ANDERSON. I think the existence of such a large debt would cause it to influence the market.

Senator Douglas, may I comment further? I should like to call the attention of the committee—and I am sorry I do not have the page number—to the statement which the Senator referred to, before the House Ways and Means Committee. We set out some charts showing the relative pricing of Federal Government securities as compared to corporate securities. I thought that the Senator might want to examine that. (Chart 8 and chart 9, appearing on pp. 18–19 of the hearings on the public debt ceiling and interest rate ceiling on bonds before the House Ways and Means Committee, June 10, 1959.)

The CHAIRMAN. Of course, as in any problem of the mutual attraction of bodies, this conforms to the Newtonian law of mechanics interpretation, that the larger bodies have an influence on smaller bodies, as well as the smaller bodies attracting the larger bodies.

Mr. Curtis?

Representative CURTIS. Thank you, Mr. Chairman.

First, let me state my personal gratification with the presentation that you have made, Mr. Secretary. I find myself in such complete accord with the philosophy you have expressed that I can only express appreciation for the manner in which it was expressed.

I think Senator Douglas is presenting a very proper and fair point of view in trying to measure the extent to which the Treasury does influence the money market. I think, however, as I have previously stated, that Secretary Humphrey always recognized that the Treasury does influence it, the issue being only over how much it influenced it. I think there is real disagreement between the Senator from Illinois and the former Secretary to the extent of this influence.

The data that has been supplied here is very helpful in trying to measure that. However, it does leave out a number of factors which bear on this question of who is competing for the savings of our people. One, of course, is real estate mortgages; consumer credit is bound

to be influenced, particularly as the Treasury goes into short-term borrowings; foreign securities, Government and otherwise; real investment, investment in real things; the stock market, certainly to the extent that the prices, over 1 year, of the total amount of stocks goes up.

Would you agree with that? And are there some other factors that bear on this that I have not mentioned?

Secretary ANDERSON. I would agree that we do compete for savings in our country. If one looks at the rapid growth which has occurred in other forms of savings institutions, these savings in volume have increased more rapidly, for example, than the volume of savings in the savings bonds.

It is recognized that anyone who seeks credit in the free market is competing with all others who seek it.

Representative CURTIS. We particularly have mutual banks and the savings and loan people who are constantly worried about how the Government manages its debt, particularly how attractive E bonds might be made, because they seem to be tapping the same market.

Of course, there is another factor in here that I think is extremely important, and certainly your paper bears on it. That is that a dollar can be an investment dollar or a consuming dollar, depending on the choice of the individual. That in itself has a great bearing on the money market, because if the attractiveness of making that dollar a consumer dollar instead of putting it into investment is great, then we have a shortage of investment dollars; this which bears on this whole market.

Secretary ANDERSON. Yes.

Representative CURTIS. I would like to get your expression on this:

The Treasury, in managing the Federal debt, of course, is trying to get the money as cheaply as possible, or so I imagine, and to that extent it does hold down interest rates the best it can. Is that not a fair statement?

Secretary ANDERSON. This is the point which I raised about the charts, indicating that we try to be as careful as we can within the context of the obligation which we have to meet the Government's debt requirements.

Representative CURTIS. In other words, just like anyone else in the market for money, the Treasury is going to try to get it at the cheapest price possible, and there are a lot of other economic factors that bear on this, other than the competition of other borrowers for this same money, that affect interest rates. Is that a fair statement?

Secretary ANDERSON. Certainly we try to borrow as cheaply as we can to secure funds.

Representative CURTIS. What I am getting at, too, is that we are talking now about the interest rate; Senator Douglas is pointing out competition is one factor, and he thinks that the competition is a little bit lopsided because the Government is such a big borrower.

Now I am directing attention to the fact that there are other economic forces at play other than competition that bear on interest rates. One of the obvious ones is, how much money is available, how much investment demand exists.

The CHAIRMAN. Would the Congressman permit me to make a clarification?

Representative CURTIS. Certainly.

The CHAIRMAN. My contention was not that there was great competition in the money market, but there was less competition than was commonly believed.

Representative CURTIS. If I knew what the word "commonly" meant, I would better understand your point.

The CHAIRMAN. Well, it was believed by Mr. George M. Humphrey, or by the Secretary in his statement before the House Ways and Means Committee.

Representative CURTIS. I might say I felt with you that Secretary Humphrey was minimizing it more than I would. On the other hand, I find, after having listened to Secretary Anderson before the Ways and Means Committee, that I think he has a pretty realistic approach to the subject.

The CHAIRMAN. I will agree there has been a big improvement in the Treasury since Mr. Anderson came there.

Representative CURTIS. Maybe we ought to quit there.

The CHAIRMAN. On the principle that when you are lying on the ground you cannot fall out of bed.

Representative CURTIS. I did not disagree with Secretary Humphrey to that extent. In fact, I am more concerned about those who seem to have the Senator's point of view that the Government just controls the price of money, and that money is not a commodity.

The CHAIRMAN. I have not unveiled my point of view yet.

Representative CURTIS. Mr. Patman says money is not a commodity. I think there can be a basic disagreement there.

But, to get on with this, of course the Treasury, in doing the best job possible, needs flexibility in handling the debt.

Is that not true, Mr. Secretary?

Secretary ANDERSON. I did not get the last. I am sorry.

Representative CURTIS. The adequacy of the job that you do in minimizing the interest rate depends on the flexibility which the Congress gives you in handling it?

Secretary ANDERSON. I think that is an important part of it; yes, sir.

Representative CURTIS. It is pretty important right now.

I think those who will not give the Secretary the flexibility that he requests in this area are the very ones that are going to increase the interest rate beyond what it would have to be.

Would the Secretary agree with that?

Secretary ANDERSON. Certainly the more pressure you bring on the short-term rate the more the short-term rate goes up, and the more the short-term rate goes up the more you influence other costs of money.

Representative CURTIS. Incidentally, the more we have to go into short-term bonds, too, the more competition we are giving in the consumer credit field and other areas of short-term financing.

Secretary ANDERSON. Yes; that is correct.

The borrowers of short-term money are more nearly the consumers.

Representative CURTIS. My time is running out, but there is one question I am going to pose and then come back to it because I think this is a very basic question which I have not had resolved to satisfac-

tion in my own mind, namely, the relation of the Federal Reserve to this problem.

I happen to feel that it is true that if the Federal Reserve comes into the money market and pegs in any sense the Federal bond interest rate, this has economic effects in other fields which are more damaging than the alternative of a rise in the cost of money. But this question has been posed, not one of absolutes as to whether it does or does not, but can the Federal Reserve Act peg the market in some temporary sense?

I think your position and the position of others is that there is no way of being intermediate about it, that either it does or it does not. But I would like to have that explored. I think it is very important that the question be explored as to whether or not in a minimal way or to a degree the Federal Reserve can help to create or be used as an instrument in creating a more stable market without having other adverse economic results.

The CHAIRMAN. Vice Chairman Patman.

Representative PATMAN. Mr. Secretary, has the Treasury put together any information which shows what proportion of its issues are purchased by a few large subscribers?

Secretary ANDERSON. Not on an individual basis, no, sir.

Representative PATMAN. Well, on any kind of basis?

Secretary ANDERSON. On a group basis we do, Congressman Patman.

Representative PATMAN. Would you make that available for the record, please?

Secretary ANDERSON. On the group basis, yes, sir.

(The material referred to is as follows:)

The attached table 5 from the June 1959 Treasury Bulletin presents the only data currently compiled by the Treasury on the allotments by investor classes on subscriptions for all Treasury marketable securities (other than regular weekly Treasury bills) from 1953 through May 1959. One further breakdown which could be compiled for recent issues, if the committee is interested, would be a breakdown by Federal Reserve districts for each of the same investor classes.

The Treasury is also compiling data which will show the number of subscribers in each of the same investor classes for each issue put out thus far in 1959 and these figures will be provided to the committee as soon as possible.

Any further breakdown of allotments could be made only by analysis of detailed records at each Federal Reserve bank and branch throughout the country. In any request for further detail on allotments it should be realized that all initial allotment figures are at best an imperfect indication of who our customers are. The allotment figures include substantial allotments to commercial banks and dealers and brokers, for example, who handle the secondary distribution of these securities to ultimate investors, sometimes within a period of a week or less. Subscribers who buy large blocks in the first instance may have very few left after they have completed their normal function of underwriting this secondary market distribution.

Reference may be made to the publication each month in the Treasury Bulletin of the ownership of each issue of Government securities by various investor classes, from which figures an analysis of investor trend in any security may be developed which more accurately reflects the distribution of each issue.

Breakdowns are available for most, but not all, of the classes for which allotment data are compiled. In addition, data are shown for each issue on a semiannual basis for New York and Chicago central Reserve city banks, Reserve city banks, country banks, and nonmember banks. Monthly data separating life from other insurance companies are also published. A copy of the ownership extract from the March 1959 Treasury Bulletin is attached.

PUBLIC DEBT OPERATIONS

TABLE 5.—Allotments by investor classes on subscriptions for public marketable securities other than regular weekly Treasury bills¹

[In millions of dollars]

Issue		Allotments by investor classes												
Date of financing	Description of security	Amount issued		U.S. Government investment accounts and Federal Reserve banks	Com-mercial banks ²	Indi-viduals ³	Insur-ance com-panies	Mutual savings banks	Cor-pora-tions ⁴	Private pen-sion and retire-ment funds	State and local governments ⁵		Dealers and brokers	All other ⁶
		For cash	In ex-change for other securities								Pension and retirement funds	Other funds		
Feb. 15, 1953	2¼ percent certificate, Feb. 15, 1954 A		8,114	3,698	2,279	187	150	55	(7)	(7)	230		152	1,363
	2¼ percent bond, Dec. 15, 1958		620	3	444	6	9	20	(7)	(7)	13		100	25
May 1, 1953	3¼ percent bond, June 15, 1978-83	1,188		118	131	261	98	99	(7)	(7)	75		158	248
June 1, 1953	2½ percent certificate, June 1, 1954 B		418	1	1	287	19	13	(7)	(7)	12		(9)	85
June 3, 1953	2.383 percent bill, Sept. 18, 1953 ¹⁰	800	4,858	1,153	2,015	98	113	77	(7)	(7)	366		162	874
July 15, 1953	2½ percent certificate, Mar. 22, 1954 C ¹⁰	5,902		(9)	711	(9)	(9)	(9)	(9)	(9)			(9)	
Aug. 15, 1953	2½ percent certificate, Aug. 15, 1954 D		2,788	175	1,499	117	82	27	411	48	1	68	115	81
Sept. 15, 1953	2½ percent certificate, Sept. 15, 1954 E		4,724	863	2,135	106	131	96	654	50	6	279	219	185
Nov. 9, 1953	2½ percent note, Mar. 15, 1957 A		2,997		2,276	42	140	86	155	3	2	40	188	65
Dec. 1, 1953	2½ percent bond, Sept. 15, 1961	2,239		50	1,296	127	190	165	93	49	19	16	170	64
	1½ percent note, Dec. 15, 1954 B		8,175	6,997	360	112	12	2	339	1	1	100	42	209
	2½ percent bond, Dec. 15, 1958 ¹¹		1,748	5	1,174	43	61	52	110	13	1	26	169	94
Feb. 15, 1954	1½ percent certificate, Feb. 15, 1955-A		7,007	3,922	1,508	152	46	7	756	6	(5)	269	123	218
Mar. 22, 1954	2½ percent bond, Nov. 15, 1961		11,177	10	8,733	209	467	218	535	92	7	163	450	293
Apr. 27, 1954	0.956-percent bill, June 24, 1954 ¹⁰	1,501		(9)	428	(9)	(9)	(9)	(9)	(9)	(9)	(9)	(9)	(9)
	0.726-percent bill, June 18, 1954 ¹⁰	1,001		(9)	915	(9)	(9)	(9)	(9)	(9)	(9)	(9)	(9)	(9)
May 17, 1954	1½ percent note, Feb. 15, 1959-A	2,205		26	1,138	175	146	139	216	36	(5)	37	219	73
	1½ percent certificate, May 17, 1955-B		2,897		1,982	41	74	23	247	23	1	103	276	130
Aug. 2, 1954	1-percent certificate, Mar. 22, 1955-C ¹⁰	3,734	3,886	1,686	986	68	28	4	558	6		294	76	180
Aug. 15, 1954	1½ percent certificate, Aug. 15, 1955-D		3,558	995	847	115	47	30	751	45	4	369	117	238
Oct. 4, 1954	2½ percent bond, Nov. 15, 1960		3,806	10	3,091	54	100	31	120	18	2	68	182	130
Dec. 15, 1954	1½ percent note, May 15, 1957-B	4,155		12	2,718	141	98	70	497	69	2	87	344	117
	1½ percent certificate, Aug. 15, 1955-D ¹²		4,919	12	4,763	57	9	1	30	13		6	6	34
	1½ percent certificate, Dec. 15, 1955-E		5,359	2,520	1,299	103	41	14	662	5	(5)	311	120	284
	2½ percent bond Aug. 15 1963		6,755		5,503	144	226	142	152	37	11	156	240	144
Feb. 15, 1955	1½ percent note, Mar. 15, 1956-A		8,472	4,012	2,385	112	63	15	1,065	36	(5)	308	256	220
	2-percent note, Aug. 15, 1957-C		3,792		2,704	69	123	43	329	3	(5)	128	232	160
	3-percent bond, Feb. 15, 1995		1,924	1	1,190	70	130	44	84	10	1	23	354	17

See footnotes at end of table.

Sept. 26, 1957	14-percent certificate, Aug. 1, 1958-C ¹⁰	933	100	756	23	1	22	2	(⁹)	10	2	15
	4-percent note, Aug. 15, 1962-B	2,000	100	1,450	93	31	50	49	6	2	175	39
Oct. 1, 1957	4-percent bond, Oct. 1, 1969	657	100	295	84	16	21	20	5	12	9	1
Nov. 29, 1957	3 3/4-percent note, Nov. 15, 1962-C	1,143	100	663	39	62	58	28	8	5	1	120
Dec. 1, 1957	3 3/4-percent certificate, Dec. 1, 1958-D		9,833	7,938	658	34	24	24	599	33	2	182
Dec. 2, 1957	3 3/4-percent bond, Nov. 15, 1974	654	100	189	43	60	98	23	29	14	10	57
Feb. 14, 1958	2 1/2-percent certificate, Feb. 14, 1959-A		9,770	5,752	1,404	171	70	18	1,085	39	2	588
	3-percent bond, Feb. 15, 1964		3,854	48	2,780	81	52	42	163	44	1	81
	3 1/2-percent bond, Feb. 15, 1990		1,727	82	520	87	176	68	113	47	10	77
Feb. 28, 1958	3-percent bond, Aug. 15, 1966	1,484	100	676	113	53	85	145	7	2	16	154
Apr. 15, 1958	2 1/2-percent note, Feb. 15, 1963-A	3,971	102	2,511	221	110	141	258	29	2	16	346
June 3, 1958	3 1/4-percent bond, May 15, 1985	1,135	100	213	86	202	76	102	31	48	9	127
June 15, 1958	1 1/4-percent certificate, May 15, 1959-B		1,817	92	571	98	18	12	570	8	(⁹)	191
	2 1/2-percent bond, Feb. 15, 1965		7,388	355	4,031	209	233	72	1,045	14	4	190
Aug. 1, 1958	1 1/2-percent certificate, Aug. 1, 1959-C		13,500	7,218	3,600	160	87	43	911	26	8	546
Aug. 6, 1958	1 1/2-percent certificate, Mar. 24, 1959-D ¹⁰	3,567		3,097	24	2	1	303	(⁹)	1	1	18
Oct. 8, 1958	3 1/4-percent bill, May 15, 1959	2,735		2,256	63	23	11	221	4	1	30	44
Oct. 10, 1958	3 1/2-percent note, Nov. 15, 1959-B	1,184	105	664	78	20	19	125	4	1	49	25
Nov. 20, 1958	2.999-percent bill, June 22, 1959 ¹⁰	2,997	(⁹)	2,871	(⁹)	(⁹)	(⁹)	(⁹)	(⁹)	(⁹)	(⁹)	(⁹)
Dec. 1, 1958	3 3/8-percent certificate, Nov. 15, 1959-E		7,711	5,086	1,090	60	44	36	798	38	5	245
	3 1/2-percent note, May 15, 1961-B		4,078	2,923	736	25	12	6	127	6	1	24
Jan. 21, 1959	3 1/4-percent note, May 15, 1960-B	2,738		2,302	48	37	17	175	5	1	11	31
Jan. 23, 1959	4-percent bond, Feb. 15, 1980	884	50	170	78	153	65	52	53	106	28	48
Feb. 15, 1959	3 3/4-percent certificate, Feb. 15, 1960		11,363	5,646	2,418	150	158	43	1,618	41	2	515
	4-percent note, Feb. 15, 1962-D		1,435	9	972	44	47	22	140	13	2	85
Feb. 16, 1959	3.293-percent bill, Sept. 21, 1959 ¹⁰	1,502	(⁹)	1,443	(⁹)	(⁹)	(⁹)	(⁹)	(⁹)	(⁹)	(⁹)	(⁹)
	4-percent note, May 15, 1963-B	1,743	100	1,331	61	17	28	52	11	1	5	79
Apr. 1, 1959	4-percent bond, Oct. 1, 1969 ²¹	619	50	335	26	35	25	26	15	12	4	37
	3.386-percent bill, Jan. 15, 1960	2,006	(⁹)	(⁹)	(⁹)	(⁹)	(⁹)	(⁹)	(⁹)	(⁹)	(⁹)	(⁹)
May 11, 1959	3.835-percent bill, Apr. 15, 1960	2,003	(⁹)	1,952	8	2	1	9	(⁹)	(⁹)	(⁹)	1
May 15, 1959	3.565-percent bill, Dec. 22, 1959 ¹⁰	1,500		539	14	4	1	227	(⁹)	(⁹)	28	667
	4-percent certificate, May 15, 1960-B		1,269	155	367	13	15	23	14	(⁹)	98	106

¹ Excludes the issuance of 1 1/2-percent Treasury notes available in exchange to holders of nonmarketable 2 3/4-percent Treasury bonds, investment series B-1975-80.
² Includes trust companies and stock savings banks.
³ Includes partnerships and personal trust accounts.
⁴ Exclusive of banks and insurance companies.
⁵ Consists of trust, sinking, and investment funds of State and local governments and their agencies.
⁶ Includes savings and loan associations, nonprofit institutions, and investments of foreign balances and international accounts in this country. Also includes corporations and private pension and retirement funds prior to July 15, 1953, financing.
⁷ Included in "All other."
⁸ Less than \$500,000.
⁹ Not available.

¹⁰ Tax-anticipation security.
¹¹ Additional offering of bonds issued Feb. 15, 1953.
¹² Additional offering of certificates issued Aug. 15, 1954.
¹³ Additional offering of bonds issued Feb. 15, 1955.
¹⁴ Additional offering of notes issued May 17, 1955.
¹⁵ Additional offering of notes issued Dec. 1, 1955.
¹⁶ Issued as a rollover of special bills maturing Jan. 16 and Feb. 15, 1957, respectively.
¹⁷ Additional offering of certificates and notes issued Feb. 15, 1957.
¹⁸ Issued in special allotment to Government investment accounts.
¹⁹ Additional offering of certificates issued Aug. 1, 1957.
²⁰ Preliminary.
²¹ Additional offering of bonds issued Oct. 1, 1967.

Source: Based on subscription and allotment reports.

(Secretary Anderson subsequently submitted the following for the record:)

SUMMARY BY INVESTOR CLASS—ALL DISTRICTS

4 percent bonds of 1980

[Dollar amounts in thousands. Bonds of 1980, dated Jan. 23, 1959, due Feb. 15, 1980, issued for cash]

Class	Number	Average subscription	Subscriptions	Average allotment	Allotments	Percent of subscriptions allotted
1. Individuals, partnerships, and personal trust accounts.....	7,653	\$21	\$160,702.5	\$10	\$76,283.5	47
2. Mutual savings banks.....	191	485	92,592.0	341	65,124.0	70
3. Insurance companies.....	388	561	217,858.5	395	153,316.5	70
4. Dealers and brokers.....	369	828	305,680.5	131	48,187.5	16
5. Pension and retirement funds of State and local governments.....	139	1,082	150,421.0	760	105,671.5	70
6. Other pension and retirement funds.....	433	171	73,978.5	123	53,043.5	72
7. State and local government funds other than pension and retirement.....	107	366	39,137.5	258	27,587.5	70
8. Commercial banks.....	1,328	350	464,947.1	128	169,735.5	37
9. Corporations other than banks and insurance companies.....	598	240	143,479.0	87	51,755.5	36
10. All others.....	919	163	150,216.5	91	83,410.5	56
11. Government investment and system accounts.....	5	10,000	50,000.0	10,000	50,000.0	100
Total.....	12,130	152	1,849,013.1	73	884,115.5	48

NOTE.—A 70-percent allotment to savings-type investors, a 35-percent allotment to commercial bank for their own account, and a 15-percent allotment to all other subscribers were made. Subscriptions up to \$25,000 were allotted in full where accompanied by 100-percent payment at the time subscriptions were entered. All other subscriptions for \$5,000 were allotted in full and subscriptions in excess of \$5,000 were allotted not less than \$5,000.

4 percent bonds of 1969 (additional issue)

[Dollar amounts in thousands. Bonds of 1969, dated Oct. 1, 1957, with interest from Apr. 1, 1959, due Oct. 1, 1969, issued for cash]

Class	Number	Average subscription	Subscriptions	Average allotment	Allotments	Percent of subscriptions allotted
1. Individuals, partnerships, and personal trust accounts.....	3,035	\$24	\$72,817.5	\$9	\$26,344.5	36
2. Mutual savings banks.....	79	478	37,735.0	311	24,591.5	65
3. Insurance companies.....	61	872	53,216.0	569	34,696.0	65
4. Dealers and brokers.....	241	755	182,056.0	152	36,591.0	20
5. Pension and retirement funds of State and local governments.....	25	731	18,285.0	477	11,931.0	65
6. Other pension and retirement funds.....	95	247	23,483.0	163	15,455.0	66
7. State and local government funds other than pension and retirement.....	31	217	6,729.5	141	4,362.5	65
8. Commercial banks.....	1,313	713	935,590.0	255	334,871.5	36
9. Corporations other than banks and insurance companies.....	196	276	54,082.5	133	26,130.5	48
10. All others.....	366	323	118,147.0	149	54,480.5	46
11. Government investment and system accounts.....	1	50,000	50,000.0	50,000	50,000.0	100
Total.....	5,443	285	1,552,141.5	114	619,454.0	40

NOTE.—A 65-percent allotment to savings-type investors, a 35-percent allotment to commercial banks for their own account, and a 20-percent allotment to all other subscribers were made. Subscriptions for \$25,000 or less from savings-type investors and commercial banks and for \$10,000 or less from all others were allotted in full. Subscriptions for more than these minimum were allotted not less than the minimums.

4 percent notes of series B-1963

[Dollar amounts in thousands. Notes of series B-1963, dated Apr. 1, 1959, due May 15, 1963, issued for cash]

Class	Number	Average subscription	Subscriptions	Average allotment	Allotments	Percent of subscriptions allotted
1. Individuals, partnerships, and personal trust accounts.....	3,978	\$20	\$80,082.0	\$15	\$60,910	76
2. Mutual savings banks.....	128	409	52,363.0	218	27,888	53
3. Insurance companies.....	88	350	30,834.0	188	16,574	54
4. Dealers and brokers.....	121	1,288	155,801.0	650	78,601	50
5. Pension and retirement funds of State and local governments.....	13	120	1,565.0	78	1,015	65
6. Other pension and retirement funds.....	160	122	19,486.0	71	11,286	58
7. State and local government funds other than pension and retirement.....	38	220	8,372.0	124	4,697	56
8. Commercial banks.....	4,035	621	2,504,322.3	330	1,330,591	53
9. Corporations other than banks and insurance companies.....	412	227	93,491.0	126	51,900	56
10. All others.....	578	184	106,122.0	103	59,578	56
11. Government investment and system accounts.....	1	100,000	100,000.0	100,000	100,000	100
Total.....	9,552	330	3,152,438.3	182	1,743,040	55

NOTE.—Subscriptions for \$100,000 or less were allotted in full and subscriptions in excess of \$100,000 were allotted 50 percent but not less than \$100,000.

3¼ percent notes of series B-1960

[Dollar amounts in thousands. Notes of series B-1960, dated Jan. 21, 1959, due May 15, 1960, issued for cash]

Class	Number	Average subscription	Subscriptions	Average allotment	Allotments	Percent of subscriptions allotted
1. Individuals, partnerships, and personal trust accounts.....	1,777	\$39	\$69,599.0	\$27	\$47,848	69
2. Mutual savings banks.....	91	358	32,558.0	188	17,082	52
3. Insurance companies.....	81	939	76,030.0	455	36,870	48
4. Dealers and brokers.....	96	664	63,748.0	322	30,908	48
5. Pension and retirement funds of State and local governments.....	3	21	63.0	21	63	100
6. Other pension and retirement funds.....	64	119	7,630.0	71	4,534	59
7. State and local government funds other than pension and retirement.....	46	499	22,953.0	250	11,482	50
8. Commercial banks.....	5,290	883	4,672,498.5	435	2,301,718	49
9. Corporations other than banks and insurance companies.....	530	672	356,111.0	331	175,478	49
10. All others.....	444	560	222,100.0	251	111,292	50
11. Government investment and system accounts.....						
Total.....	8,422	656	5,623,200.5	325	2,737,275	50

NOTE.—Subscriptions for \$100,000 or less were allotted in full and subscriptions in excess of \$100,000 were allotted 47 percent but not less than \$100,000.

4 percent notes of series D-1962

[Dollar amounts in thousands. Notes of series D-1962, dated Feb. 15, 1959, due Feb. 15, 1962. Issued in exchange for 2½ percent certificates of indebtedness of series A-1959, and 1½ percent notes of series A-1959]

Class	Number	Subscriptions and allotments	Average subscription and allotment
1. Individuals, partnerships, and personal trust accounts..	1, 690.	\$44, 187	\$26
2. Mutual savings banks.....	75	22, 250	297
3. Insurance companies.....	99	47, 119	476
4. Dealers and brokers.....	56	26, 463	473
5. Pension and retirement funds of State and local governments.....	8	2, 381	298
6. Other pension and retirement funds.....	111	12, 860	116
7. State and local government funds other than pension and retirement.....	258	84, 803	329
8. Commercial banks.....	4, 992	972, 091	195
9. Corporations other than banks and insurance companies.	440	140, 226	319
10. All others.....	439	75, 424	172
11. Government investment and system accounts.....	2	7, 232	3, 616
Total.....	8, 170	1, 435, 036	176

4 percent certificates of indebtedness of series B-1960

[Dollar amounts in thousands. Certificates of series B-1960, dated May 15, 1959, due May 15, 1960. Issued in exchange for certificates of indebtedness of series B-1959]

Class	Number	Subscriptions and allotments	Average subscription and allotment
1. Individuals, partnerships, and personal trust accounts..	1, 132	\$32, 991	\$29
2. Mutual savings banks.....	30	23, 450	782
3. Insurance companies.....	35	14, 704	420
4. Dealers and brokers.....	36	106, 437	2, 957
5. Pension and retirement funds of State and local governments.....	2	105	52
6. Other pension and retirement funds.....	110	13, 642	124
7. State and local government funds other than pension and retirement.....	167	97, 626	585
8. Commercial banks.....	1, 381	366, 865	266
9. Corporations other than banks and insurance companies.	460	266, 119	579
10. All others.....	288	268, 387	932
11. Government investment and System accounts.....	3.	79, 135	26, 378
Total.....	3, 644	1, 269, 461	348

4¾ percent notes of series A-1964

[Dollar amounts in thousands. Notes of series A-1964, dated July 20, 1959, due May 15, 1964. Issued in exchange for 1½ percent certificates of indebtedness of series C-1959, and 4 percent notes of series A-1961]

Class	Number	Subscriptions and allotments	Average subscription and allotment
1. Individuals, partnerships, and personal trust accounts..	912	\$32, 004	\$35
2. Mutual savings banks.....	79	48, 463	613
3. Insurance companies.....	66	25, 477	386
4. Dealers and brokers.....	93	189, 814	2, 041
5. Pension and retirement funds of State and local governments.....	5	31, 530	6, 306
6. Other pension and retirement funds.....	64	10, 347	162
7. State and local government funds other than pension and retirement.....	122	67, 868	556
8. Commercial banks.....	2, 798	802, 513	287
9. Corporations other than banks and insurance companies.	233	179, 585	754
10. All others.....	220	134, 214	610
11. Government investment accounts.....	2	14, 746	7, 373
Total (except for system account).....	4, 594	1, 536, 561	334
System account.....		2, 642, 733	
Grand total.....		4, 179, 294	

3¾ percent certificates of indebtedness of series A-1960

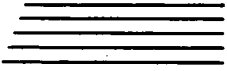
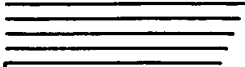
[Dollar amounts in thousands. Certificates of series A-1960, dated Feb. 15, 1959, due Feb. 15, 1960. Issued in exchange for 2½ percent certificates of indebtedness of series A-1959, and 1½ percent notes of series A-1959]

Class	Number	Subscriptions and allotments	Average subscription and allotment
1. Individuals, partnerships, and personal trust accounts.....	3,632	\$150,224	\$41
2. Mutual savings banks.....	91	43,028	473
3. Insurance companies.....	156	157,614	1,010
4. Dealers and brokers.....	172	206,914	1,203
5. Pension and retirement funds of State and local governments.....	4	2,230	558
6. Other pension and retirement funds.....	179	40,937	229
7. State and local government funds other than pension and retirement.....	483	515,284	1,067
8. Commercial banks.....	4,583	2,417,695	528
9. Corporations other than banks and insurance companies.....	1,640	1,617,829	986
10. All others.....	816	703,129	862
11. Government investment accounts.....	1	749	749
Total (except for system account).....	11,757	5,855,633	498
System account.....		5,506,993	
Grand total.....		11,362,626	

4¾ percent notes of series C-1960

[Dollar amounts in thousands. Notes of series C-1960, dated Aug. 1, 1959, due Aug. 15, 1960. Issued in exchange for 1½ percent certificates of indebtedness of series C-1959, and 4 percent notes of series A-1961]

Class	Number	Subscriptions and allotments	Average subscription and allotment
1. Individuals, partnerships, and personal trust accounts....	2,792	\$108,885	\$39
2. Mutual savings banks.....	67	38,028	568
3. Insurance companies.....	107	74,902	700
4. Dealers and brokers.....	161	278,202	1,728
5. Pension and retirement funds of State and local governments.....	6	8,491	1,415
6. Other pension and retirement funds.....	132	18,027	137
7. State and local government funds other than pension and retirement.....	431	491,395	1,140
8. Commercial banks.....	4,398	1,374,877	313
9. Corporations other than banks and insurance companies.....	1,154	1,298,623	1,125
10. All others.....	722	364,252	505
11. Government investment accounts.....	3	4,834	1,611
Total (except for system account).....	9,973	4,060,516	407
System account.....		5,500,000	
Grand total.....		9,560,516	

EXTRACT FROM THE
TREASURY 
 *BULLETIN*



OWNERSHIP OF
UNITED STATES
GOVERNMENT
SECURITIES
DEC. 31, 1958

UNITED STATES TREASURY DEPARTMENT
OFFICE OF THE SECRETARY
MARCH-1959

1113

Table 3.- Estimated Ownership of Federal Securities

(Par values $\frac{1}{2}$ in billions of dollars)

End of month	Total Federal securities outstanding $\frac{2}{2}$	Held by banks			U. S. Government investment accounts $\frac{4}{4}$	Held by private nonbank investors								
		Total	Commer- cial banks $\frac{3}{3}$	Federal Reserve Banks		Total	Individuals $\frac{5}{5}$			Insurance companies	Mutual savings banks	Corpora- tions $\frac{6}{6}$	State and local govern- ments $\frac{7}{7}$	Miscel- laneous investors $\frac{8}{8}$
							Total	Savings bonds	Other					
1939-December.....	47.6	18.4	15.9	2.5	6.5	22.7	10.1	1.9	8.2	6.3	3.1	2.2	.4	.7
1940-June.....	48.5	18.6	16.1	2.5	7.1	22.8	10.1	2.6	7.5	6.5	3.1	2.1	.4	.7
December.....	50.9	19.5	17.3	2.2	7.6	23.9	10.6	2.8	7.8	6.9	3.2	2.0	.5	.7
1941-June.....	55.3	21.8	19.7	2.2	8.5	25.0	11.2	3.6	7.6	7.1	3.4	2.0	.6	.7
December.....	64.3	23.7	21.4	2.3	9.5	31.0	13.6	5.4	8.2	8.2	3.7	4.0	.7	.9
1942-June.....	77.0	28.7	26.0	2.6	10.6	37.7	17.8	9.1	8.7	9.2	3.9	4.9	.9	1.1
December.....	112.5	47.3	41.1	6.2	12.2	53.0	23.7	13.4	10.3	11.3	4.5	10.1	1.0	2.3
1943-June.....	140.8	59.4	52.2	7.2	14.3	67.0	30.9	19.2	11.7	13.1	5.3	12.9	1.5	3.4
December.....	170.1	71.5	59.9	11.5	16.9	81.7	37.6	24.7	12.9	15.1	6.1	16.4	2.1	4.4
1944-June.....	202.6	83.3	68.4	14.9	19.1	100.2	46.1	31.2	14.9	17.3	7.3	20.2	3.2	6.1
December.....	232.1	96.5	77.7	18.8	21.7	114.0	53.3	36.2	17.1	19.6	8.3	21.4	4.3	7.0
1945-June.....	259.1	106.0	84.2	21.8	24.9	128.2	59.1	40.7	18.5	22.7	9.6	23.3	5.3	8.3
December.....	278.7	115.0	90.8	24.3	27.0	136.6	64.1	42.9	21.2	24.0	10.7	22.2	6.5	9.1
1946-February 9/..	279.8	116.7	93.8	22.9	28.0	135.1	64.1	43.3	20.8	24.4	11.1	19.9	6.7	8.9
June.....	269.9	108.2	84.4	23.8	29.1	132.6	63.3	43.5	19.9	24.9	11.5	17.8	6.5	8.6
December.....	259.5	97.9	74.5	23.3	30.9	130.7	64.2	44.2	20.1	24.9	11.8	15.3	6.3	8.1
1947-June.....	258.4	91.9	70.0	21.9	32.8	133.7	66.6	45.5	21.1	24.6	12.1	13.7	7.1	9.6
December.....	257.0	91.3	68.7	22.6	34.4	131.3	65.7	46.2	19.4	23.9	12.0	14.1	7.3	8.4
1948-June.....	252.4	85.9	64.6	21.4	35.8	130.7	65.8	47.1	18.6	22.8	12.0	13.6	7.8	8.7
December.....	252.9	85.8	62.5	23.3	37.3	129.7	65.5	47.8	17.6	21.2	11.5	14.8	7.9	8.9
1949-June.....	252.8	82.4	63.0	19.3	38.3	132.2	66.6	48.8	17.8	20.5	11.6	15.8	8.0	9.6
December.....	257.2	85.7	66.8	18.9	39.4	132.1	66.3	49.3	17.0	20.1	11.4	16.8	8.1	9.4
1950-June.....	257.4	83.9	65.6	18.3	37.8	135.6	67.4	49.9	17.6	19.8	11.6	18.4	8.7	9.7
December.....	256.7	82.6	61.8	20.8	39.2	134.9	66.3	49.6	16.7	18.7	10.9	19.7	8.8	10.5
1951-June.....	255.3	81.4	58.4	23.0	41.0	132.9	65.4	49.1	16.3	17.1	10.2	20.1	9.4	10.7
December.....	259.5	85.4	61.6	23.8	42.3	131.8	64.6	49.1	15.5	16.5	9.8	20.7	9.6	10.6
1952-June.....	259.2	84.0	61.1	22.9	44.3	130.8	64.8	49.0	15.7	15.7	9.6	18.8	10.4	11.6
December.....	267.4	88.1	63.4	24.7	45.9	133.4	65.1	49.2	16.0	16.1	9.5	19.9	11.1	11.7
1953-June.....	266.1	83.6	58.8	24.7	47.6	135.0	66.1	49.3	16.9	16.0	9.5	18.6	12.0	12.8
December.....	275.2	89.6	63.7	25.9	48.3	137.3	64.9	49.4	15.5	15.8	9.2	21.5	12.7	13.2

1954-June.....	271.3	88.7	63.6	25.0	49.3	133.3	64.8	49.5	15.3	15.3	9.1	16.6	13.9	13.7
December.....	278.8	94.1	69.2	24.9	49.6	135.1	63.6	50.0	13.7	15.0	8.8	19.2	14.4	13.9
1955-June.....	274.4	87.1	63.5	23.6	50.5	136.7	65.6	50.2	15.4	14.8	8.7	18.5	14.7	14.4
December.....	280.8	86.8	62.0	24.8	51.7	142.3	65.8	50.2	15.6	14.3	8.5	23.0	15.1	15.6
1956-June.....	272.8	80.8	57.1	23.8	53.5	138.5	67.7	50.3	17.4	13.3	8.4	17.1	15.7	16.3
December.....	276.7	84.2	59.3	24.9	54.0	138.5	67.3	50.1	17.2	12.8	8.0	18.2	16.1	16.1
1957-March.....	275.1	81.3	58.1	23.1	54.2	139.7	68.4	49.6	18.8	12.6	8.1	17.7	16.6	16.4
June.....	270.6	78.9	55.8	23.0	55.6	136.2	67.8	49.1	18.7	12.3	7.9	15.4	16.9	16.0
July.....	272.6	80.2	56.8	23.4	55.2	137.3	67.9	48.9	19.0	12.3	7.9	16.0	16.9	16.2
August.....	274.0	80.1	56.6	23.5	55.8	138.0	68.4	48.8	19.6	12.2	7.9	16.5	17.1	15.9
September....	274.5	81.6	58.3	23.3	55.4	137.4	68.5	48.6	19.9	12.2	7.9	15.7	17.2	15.9
October.....	274.2	81.4	58.1	23.3	55.4	137.3	67.8	48.4	19.4	12.2	7.8	15.9	17.2	16.3
November.....	274.9	81.9	58.2	23.7	55.3	137.6	67.6	48.3	19.3	12.1	7.6	16.5	17.3	16.5
December.....	275.0	83.3	59.1	24.2	55.2	136.4	66.8	48.2	18.6	12.0	7.6	16.5	17.0	16.5
1958-January.....	274.7	82.0	58.6	23.3	55.1	137.6	67.1	48.2	18.9	12.0	7.6	17.3	17.3	16.2
February.....	274.8	82.7	59.4	23.2	55.4	136.7	66.8	48.2	18.6	11.9	7.6	17.2	17.3	15.9
March.....	272.7	83.0	59.4	23.6	55.4	134.3	66.9	48.1	18.7	11.8	7.6	15.4	17.3	15.4
April.....	275.2	86.9	63.2	23.7	55.2	133.1	66.4	48.1	18.3	11.8	7.6	14.6	17.1	15.7
May.....	275.7	87.7	63.6	24.2	55.8	132.3	66.1	48.1	18.1	11.7	7.5	14.7	17.0	15.4
June.....	276.4	90.3	64.9	25.4	55.9	130.2	65.7	48.0	17.7	11.7	7.4	13.3	16.9	15.2
July.....	275.6	89.4	65.0	24.5	55.6	130.5	65.3	47.9	17.4	11.8	7.4	13.9	17.0	15.0
August.....	278.6	91.8	66.4	25.3	56.0	130.8	65.0	47.9	17.0	11.9	7.5	14.6	17.0	14.9
September....	276.8	90.4	65.5	25.0	55.6	130.7	64.8	47.9	16.9	11.9	7.4	14.3	17.0	15.3
October.....	280.3	92.1	66.7	25.4	55.1	133.1	64.9	47.8	17.1	12.1	7.4	15.9	17.2	15.8
November.....	283.2	93.9	67.7	26.2	54.8	134.5	64.9	47.8	17.1	12.1	7.3	16.9	17.2	16.0
December p....	283.0	93.6	67.2	26.3	54.4	135.1	65.1	47.7	17.4	12.1	7.3	16.9	17.3	16.5

Source: Office of the Secretary, Debt Analysis Staff.

- 1/ United States savings bonds, Series A-F and J, are included at current redemption value.
- 2/ Securities issued or guaranteed by the U. S. Government, excluding guaranteed securities held by the Treasury. For amounts subject to statutory debt limitation, see page 1.
- 3/ Consists of commercial banks, trust companies, and stock savings banks in the United States and in Territories and island possessions. Figures exclude securities held in trust departments.
- 4/ Holdings by Federal land banks are included under "Miscellaneous investors" instead of "U. S. Government investment accounts" after June 26, 1947, when the proprietary interest of the United States in these banks ended.
- 5/ Includes partnerships and personal trust accounts. Nonprofit

institutions and corporate pension trust funds are included under "Miscellaneous investors."

- 6/ Exclusive of banks and insurance companies.
- 7/ Consists of trust, sinking, and investment funds of State and local governments and their agencies, and Territories and island possessions.
- 8/ Includes savings and loan associations, nonprofit institutions, corporate pension trust funds, dealers and brokers, and investments of foreign balances and international accounts in this country. Beginning December 1946, includes investments by the International Bank for Reconstruction and Development and the International Monetary Fund in special noninterest-bearing notes issued by the U. S. Government.
- 9/ Immediate postwar debt peak.
- p Preliminary.

The Treasury Survey of Ownership covers securities issued by the United States Government and by Federal agencies. The banks and insurance companies included in the Survey account for approximately 95 percent of such securities held by all banks and insurance companies in the United States. Data were first published for March 31, 1941, in the May 1941 "Treasury Bulletin".

Distribution of ownership by types of banks and insurance companies is published each month. Holdings by commercial banks distributed according to Federal Reserve member-bank classes and nonmember banks are published for June 30 and December 31. Holdings by corporate pension trust funds are published quarterly and first appeared in the March 1954 Bulletin for quarters beginning December 31, 1949.

Section I.- Securities Issued or Guaranteed by the United States Government
Table 1.- Summary of All Securities

(Par values - in millions of dollars)

Classification	Total amount outstanding ^{1/}	Held by investors covered in Treasury Survey				U. S. Government investment accounts and Federal Reserve Banks	Held by all other investors ^{4/}	Memorandum: Held by 10,239 corporate pension trust funds ^{5/}
		6,481 commercial banks ^{2/ 3/}	516 mutual savings banks ^{2/}	Insurance companies				
				306 life	546 fire, casualty, and marine			
Interest-bearing securities:								
Public marketable.....	175,695	58,925	6,073	4,712	4,251	33,026	68,708	1,514
Public nonmarketable ^{6/}	60,412	1,014 ^{7/}	1,170	2,223	385	2,877	52,744	390
Special issues.....	44,840	-	-	-	-	44,840	-	-
Total interest-bearing securities.....	280,947	59,940	7,243	6,935	4,636	80,743	121,452	1,904
Matured debt and debt bearing no interest ^{8/}	2,084							
Total securities issued or guaranteed by the U. S. Government ^{9/}.....	283,031							

Footnotes at end of Table 4.

Table 2.- Summary of Interest-Bearing Public Marketable Securities

(Par values - in millions of dollars)

Classification	Total amount outstanding	Held by investors covered in Treasury Survey				U. S. Government investment accounts and Federal Reserve Banks	Held by all other investors 4/	Memorandum: Held by 10,239 corporate pension trust funds 5/
		6,481 commercial banks 2/ 3/	516 mutual savings banks 2/	Insurance companies				
				306 life	546 fire, casualty, and marine			
Type of security:								
Issued by U. S. Government:								
Treasury bills.....	29,748	5,194	139	456	270	2,363	21,326	291
Certificates of indebtedness.....	36,364	6,686	115	53	178	19,196	10,137	71
Treasury notes.....	26,072	12,285	538	61	670	4,213	8,304	119
Treasury bonds.....	83,352	34,743	5,268	4,124	3,129	7,195	28,894	1,030
Panama Canal bonds.....	50	11	-	-	2	-	38	*
Guaranteed by U. S. Government 9/.....	108	7	13	19	1	59	10	2
Total.....	175,695	58,925	6,073	4,712	4,251	33,026	68,708	1,514
Call classes:								
Due or first becoming callable:								
Within 1 year.....	81,339	18,254	540	612	1,040	22,950	37,943	455
1 to 5 years.....	50,013	28,550	1,645	537	1,727	5,036	12,516	333
5 to 10 years.....	35,717	11,410	3,149	2,761	1,188	4,210	12,998	305
10 to 15 years.....	657	122	51	23	28	104	329	18
15 to 20 years.....	2,257	130	193	105	68	244	1,517	110
20 years and over.....	5,603	451	482	654	199	422	3,395	291
Various (Federal Housing Administration debentures).....	108	7	13	19	1	59	10	2
Total.....	175,695	58,925	6,073	4,712	4,251	33,026	68,708	1,514
Tax status: 10/								
Wholly exempt from Federal income taxes.....	50	11	-	-	2	-	38	*
Partially exempt from Federal income taxes.....	1,485	1,310	*	*	32	*	142	-
Subject to Federal income taxes 11/.....	174,159	57,605	6,072	4,712	4,216	33,026	68,528	1,514
Total.....	175,695	58,925	6,073	4,712	4,251	33,026	68,708	1,514

Footnotes at end of Table 4.

Section I.- Securities Issued or Guaranteed by the United States Government

Table 3.- Interest-Bearing Public Marketable Securities by Issues

(Par value - in millions of dollars)

Issue (Tax status <u>10/</u> is shown in parentheses)	Total amount outstanding	Held by investors covered in Treasury Survey				Held by all other investors <u>4/</u>	Memorandum: Held by 10,239 corporate pension trust funds <u>5/</u>	
		6,481 commercial banks <u>2/ 3/</u>	516 mutual savings banks <u>2/</u>	Insurance companies				U. S. Government investment accounts and Federal Reserve Banks
				306 life	546 fire, casualty, and marine			
Treasury bills:								
Regular weekly.....(taxable)	24,016	3,466	95	379	222	2,331	17,523	257
Tax anticipation.....(taxable)	2,997	1,051	17	10	19	4	1,897	16
Other.....(taxable)	2,735	678	27	67	29	28	1,906	18
Total Treasury bills.....	29,748	5,194	139	456	270	2,363	21,326	291
Certificates of indebtedness:								
2-1/2* February 1959-A.....(taxable)	9,770	1,279	25	5	51	5,657	2,753	30
1-1/2 March 1959-D <u>12/</u>.....(taxable)	3,567	1,889	1	14	8	2	1,653	1
1-1/4 May 1959-B.....(taxable)	1,817	420	7	*	18	112	1,260	12
1-5/8 August 1959-C.....(taxable)	13,500	2,375	27	7	49	8,313	2,729	11
3-3/8 November 1959-E.....(taxable)	7,711	723	55	26	52	5,112	1,741	16
Total certificates of indebtedness.....	36,364	6,686	115	53	178	19,196	10,137	71
Treasury notes:								
1-7/8* February 1959-A.....(taxable)	5,102	2,063	24	6	157	48	2,804	26
3-1/2 November 1959-B.....(taxable)	1,184	369	20	4	24	106	660	15
3-1/2 May 1960-A.....(taxable)	2,406	1,058	40	2	88	269	948	14
3-5/8 May 1961-B.....(taxable)	4,078	582	15	4	22	2,926	329	8
<u>4</u> August 1961-A.....(taxable)	2,609	1,091	90	2	56	229	1,140	16
<u>4</u> 3-5/8 February 1962-A.....(taxable)	647	170	7	-	24	323	124	3
<u>4</u> August 1962-B.....(taxable)	2,000	1,292	119	3	50	88	449	17
3-3/4 November 1962-C.....(taxable)	1,143	699	53	1	66	95	229	3
2-5/8 February 1963-A.....(taxable)	3,971	3,191	83	10	48	126	514	9
1-1/2 April 1959-EA.....(taxable)	119	31	*	-	2	3	81	1
1-1/2 October 1959-ED.....(taxable)	99	38	2	-	6	*	54	*
1-1/2 April 1960-EA.....(taxable)	198	95	*	*	12	-	91	*
1-1/2 October 1960-ED.....(taxable)	278	149	1	*	13	-	114	*

1-1/2	April	1961-EA.....(taxable)	144	102	1	*	9	-	32	1
1-1/2	October	1961-ED.....(taxable)	332	203	*	2	21	-	106	*
1-1/2	April	1962-EA.....(taxable)	551	344	18	3	41	-	145	4
1-1/2	October	1962-ED.....(taxable)	590	427	21	7	6	-	129	2
1-1/2	April	1963-EA.....(taxable)	533	335	42	15	18	-	123	1
1-1/2	October	1963-ED.....(taxable)	87	46	1	-	7	-	34	*
Total Treasury notes.....			26,072	12,285	538	61	670	4,213	8,304	119
Treasury bonds:										
2-1/4	June	1959-62.....(taxable)	5,267	2,538	162	31	261	495	1,781	37
2-1/4	December	1959-62.....(taxable)	3,456	1,336	78	62	141	738	1,100	16
2-1/8	November	1960.....(taxable)	3,806	2,663	16	*	87	25	1,015	26
2-3/4	December	1960-65.....(partially)	1,485	1,310	*	*	32	*	142	-
2-3/4	September	1961.....(taxable)	2,239	1,315	97	5	139	44	639	28
2-1/2	November	1961.....(taxable)	11,177	7,469	236	34	390	164	2,885	78
2-1/2	June	1962-67.....(taxable)	2,112	764	212	155	127	268	585	26
2-1/2	August	1963.....(taxable)	6,755	4,579	148	22	272	54	1,679	42
2-1/2	December	1963-68.....(taxable)	2,820	654	444	271	198	425	829	56
3	February	1964.....(taxable)	3,854	2,786	74	2	63	58	873	20
2-1/2	June	1964-69.....(taxable)	3,745	779	859	361	185	451	1,109	48
2-1/2	December	1964-69.....(taxable)	3,819	766	632	493	154	524	1,250	47
2-5/8	February	1965.....(taxable)	6,896	4,014	144	27	242	528	1,941	41
2-1/2	March	1965-70.....(taxable)	4,700	487	617	821	144	1,230	1,401	40
2-1/2	March	1966-71.....(taxable)	2,948	198	304	775	90	700	881	32
3	August	1966.....(taxable)	1,484	905	84	2	36	106	350	12
2-1/2	June	1967-72.....(taxable)	1,840	108	159	82	41	150	1,299	16
2-1/2	September	1967-72.....(taxable)	2,716	1,220	158	16	117	237	969	13
2-1/2	December	1967-72.....(taxable)	3,715	148	118	182	116	226	2,925	36
4	October	1969.....(taxable)	657	122	51	23	28	104	329	18
3-7/8	November	1974.....(taxable)	654	78	118	22	31	100	305	44
3-1/4	June	1978-83.....(taxable)	1,604	53	74	83	37	144	1,212	65
3-1/4	May	1985.....(taxable)	1,135	198	83	178	34	119	523	20
3-1/2	February	1990.....(taxable)	1,727	174	162	234	96	126	935	113
3	February	1995.....(taxable)	2,741	79	237	241	69	178	1,937	157
Total Treasury bonds.....			83,352	34,743	5,268	4,124	3,129	7,195	28,894	1,030

Footnotes at end of Table 4.

(Continued on following page)

Section I. - Securities Issued or Guaranteed by the United States Government
Table 3.- Interest-Bearing Public Marketable Securities by Issues - (Continued)

(Par values - in millions of dollars)

Issue (Tax status <u>10/</u> is shown in parentheses)	Total amount outstanding	Held by investors covered in Treasury Survey				Held by all other investors <u>4/</u>	Memorandum: Held by 10,239 corporate pension trust funds <u>5/</u>	
		6,481 commercial banks <u>2/ 3/</u>	516 mutual savings banks <u>2/</u>	Insurance companies				U. S. Government investment accounts and Federal Reserve Banks
				306 life	546 fire, casualty, and marine			
Panama Canal bonds.....(wholly)	50	11	-	-	2	-	38	•
Guaranteed securities: <u>2/</u> Federal Housing Administration debentures.....(taxable <u>13/</u>)	108	7	13	19	1	59	10	2
Total public marketable securities.....	175,695	58,925	6,073	4,712	4,251	33,026	68,708	1,514

Footnotes at end of Table 4.

Table 4.- Interest-Bearing Public Nonmarketable Securities by Issues

(Par values - in millions of dollars)

Issue (Tax status <u>10/</u> is shown in parentheses)	Total amount outstanding	Held by investors covered in Treasury Survey				Held by all other investors <u>4/</u>	Memorandum: Held by 10,239 corporate pension trust funds <u>5/</u>	
		6,481 commercial banks <u>2/ 3/</u>	516 mutual savings banks <u>2/</u>	Insurance companies				U. S. Government investment accounts and Federal Reserve Banks
				306 life	546 fire, casualty, and marine			
United States savings bonds:								
Series E <u>6/</u>.....(taxable)	38,206	-	•	•	•	2	38,205	69
Series F <u>6/</u>.....(taxable)	1,025	178	1	7	42	•	796	44

Series G.....(taxable)	4,963	355	188	85	142	9	4,185	107
Series H.....(taxable)	4,383	-	*	*	*	*	4,382	2
Series J ^{6/}.....(taxable)	717	*	-	2	8	2	705	13
Series K.....(taxable)	1,898	2	31	8	26	5	1,826	38
Total United States savings bonds.....	51,192	535	220	102	218	18	50,099	272
<u>Other U. S. securities:</u>								
Depository bonds.....(taxable)	203	203 ^{7/}	*	-	-	-	-	-
Treasury bonds:								
Investment Series A.....(taxable)	708	145	68	223	24	100	148	12
Investment Series B.....(taxable)	8,308	130	882	1,898	144	2,759	2,497	107
Total other U. S. securities.....	9,220	479 ^{7/}	950	2,121	167	2,859	2,644	119
Total public nonmarketable securities.....	60,412	1,014 ^{7/}	1,170	2,223	385	2,877	52,744	390

^{1/} Includes certain obligations not subject to statutory debt limitation. For amount subject to limitation, see page 1.

^{2/} Excludes trust departments.

^{3/} Includes trust companies and, beginning with figures for July 1949, also includes stock savings banks. Previously, those banks were reported as a separate classification.

^{4/} Includes those banks and insurance companies not reporting in the Treasury Survey.

^{5/} Consists of corporate pension trust funds and profit sharing plans which involve retirements benefits. The data are compiled from quarterly reports by trustees of funds which account for approximately 90 percent of United States Government securities held by all corporate pension trust funds. Since the data are not available each month, the regular monthly Survey includes holdings by these funds under "Held by all other investors." The quarterly data are presented as supplemental information in a memorandum column accompanying the Survey for each reporting date, beginning with December 31, 1953. The corresponding information from earlier reports, beginning with December 31, 1949, is summarized on page 30 of the March 1954 "Treasury Bulletin."

^{6/} United States savings bonds, Series E, F, and J, are shown at current redemption value. They were reported at maturity value by the banks and insurance companies included in the Treasury Survey but have been adjusted to current redemption value for use in this statement.

^{7/} Includes \$75 million depository bonds held by commercial banks not included in the Treasury Survey.

^{8/} Holdings by reporting investors not available.

^{9/} Excludes guaranteed securities held by the Treasury.

^{10/} Federal securities fall into three broad classes with respect to the imposition of Federal income taxes on income derived from them. "Wholly" tax-exempt securities are those with the income exempt from both normal tax and surtax. "Partially" tax-exempt securities are those with the income exempt from the normal tax except that in the case of partially tax-exempt Treasury bonds, interest derived from \$5,000 of principal amount owned by any one holder is also exempt from the surtax. "Taxable" securities are those with the income subject to normal tax and surtax.

Remaining footnotes on following page.

**Section II - Interest-Bearing Securities Issued by Federal Agencies but
Not Guaranteed by the United States Government**

(Par values - in millions of dollars)

Issue (Tax status <u>10/</u> is shown in parentheses)	Total amount outstand- ing <u>11/</u>	Held by investors covered in Treasury Survey				U. S. Government investment accounts and Federal Reserve Banks	Held by all other investors <u>12/</u>	Memorandum: Held by 10,239 corporate pension trust funds <u>2/</u>
		6,481 commercial banks <u>2/ 3/</u>	516 mutual savings banks <u>2/</u>	Insurance companies				
				306 life	546 fire, casualty, and marine			
Banks for cooperatives:								
1.70% March 1959 (Debentures)...(taxable)	72	21	2	-	-	-	49	-
2.85 April 1959 (Debentures)...(taxable)	82	27	4	*	1	-	51	1
3-1/2 June 1959 (Debentures)...(taxable)	98	23	6	*	1	-	68	*
Total banks for cooperatives securities.....	<u>252</u>	<u>71</u>	<u>11</u>	<u>*</u>	<u>2</u>	<u>-</u>	<u>167</u>	<u>1</u>
Federal home loan banks: <u>15/</u>								
1-1/4% January 1959 (Notes).....(taxable)	80	20	1	1	*	-	58	*
1.60 February 1959 (Notes).....(taxable)	116	35	2	4	1	-	74	1
3-1/4 March 1959 (Notes).....(taxable)	130	38	2	1	1	-	89	2
3-1/2 April 1959 (Notes).....(taxable)	106	24	6	*	*	-	75	1
3-1/8 April 1963 (Bonds).....(taxable)	282	94	12	1	1	-	175	*
Total Federal home loan bank securities.....	<u>714</u>	<u>211</u>	<u>23</u>	<u>6</u>	<u>4</u>	<u>-</u>	<u>470</u>	<u>4</u>
Federal intermediate credit banks:								
Debentures.....(taxable)	<u>1,116</u>	<u>347</u>	<u>30</u>	<u>9</u>	<u>16</u>	<u>1</u>	<u>712</u>	<u>3</u>

Federal land banks: 16/										
4-5/8	February 1959	(Bonds)....(taxable)	140	40	5	*	4	-	90	2
2-1/4	May 1959	(Bonds)....(taxable)	71	31	4	*	2	-	34	1
3-1/2	May 1959	(Bonds)....(taxable)	120	37	8	*	3	-	72	1
1-3/4	October 1959	(Bonds)....(taxable)	164	73	5	-	2	-	84	1
2-1/4	February 1960	(Bonds)....(taxable)	124	68	2	*	2	-	52	1
2-1/2	June 1960	(Bonds)....(taxable)	106	51	7	*	3	-	45	2
3-3/8	April 1961	(Bonds)....(taxable)	83	35	6	1	2	-	40	1
4	September 1961	(Bonds)....(taxable)	120	42	7	*	2	-	70	2
4	May 1962	(Bonds)....(taxable)	125	20	5	1	1	-	98	5
2-3/4	May 1963	(Bonds)....(taxable)	122	73	6	1	1	-	41	2
3-1/4	May 1966	(Bonds)....(taxable)	108	40	10	*	4	-	54	3
4-1/8	February 1967-72	(Bonds)....(taxable)	72	3	5	6	1	-	58	12
4-1/2	October 1967-70	(Bonds)....(taxable)	75	4	10	1	4	-	56	8
4-5/8	July 1969	(Bonds)....(taxable)	60	2	7	1	1	-	48	7
3-1/2	April 1970	(Bonds)....(taxable)	83	9	9	1	1	-	63	4
3-1/2	May 1971	(Bonds)....(taxable)	60	1	6	3	2	-	49	11
3-7/8	September 1972	(Bonds)....(taxable)	109	*	5	5	3	-	95	22
Total Federal land bank securities.....			1,743	529	108	21	37	-	1,048	84
Federal National Mortgage Association:										
3	February 1959	(Debentures)..(taxable)	150	35	4	2	6	-	103	*
1.65	April 1959	(Debentures)..(taxable)	100	33	3	*	2	-	62	*
2	June 1959	(Debentures)..(taxable)	100	32	5	1	*	-	61	*
3-7/8	August 1959	(Debentures)..(taxable)	100	29	3	*	2	-	67	*
3-5/8	August 1960	(Notes).....(taxable)	797	460	50	2	17	2	267	4
3-1/2	February 1962	(Debentures)..(taxable)	200	65	24	1	6	-	105	7
3-1/4	March 1963	(Debentures)..(taxable)	150	58	15	*	4	-	73	3
4-1/8	November 1963	(Debentures)..(taxable)	100	21	10	1	5	-	62	2
4-3/8	June 1965	(Debentures)..(taxable)	100	31	17	1	4	-	48	6
3-5/8	March 1968	(Debentures)..(taxable)	100	19	8	1	4	-	68	3
Total Federal National Mortgage Association securities.....			1,897	782	139	10	50	2	914	28

Footnotes 1 through 10 on preceding page.

11/ Includes Federal Housing Administration debentures; see footnote 13/.

12/ Tax anticipation series.

13/ A small indeterminate amount of these debentures is partially tax-exempt.

14/ Includes only publicly offered issues.

15/ The proprietary interest of the United States in these banks ended in July 1951.

16/ The proprietary interest of the United States in these banks ended in June 1947.

* Less than \$500,000.

The tables which follow provide an analysis of the security holdings of commercial banks reporting in the Treasury survey of ownership of securities issued by the United States Government and by Federal agencies. The figures show the total holdings distributed according to Federal Reserve member-bank classes and nonmember banks.

This analysis of commercial bank ownership was first published in the May 1944 issue of the "Treasury Bulletin," based on the survey data for December 31, 1943. It has appeared at semiannual or quarterly intervals since that time, and is now being published for the June 30 and December 31 survey data.

Section I.- Interest-Bearing Securities Issued or Guaranteed by the United States Government

Table 1.- Summary of all Securities

(Par values - in millions of dollars)

Classification	Held by 6,481 commercial banks 1/	Federal Reserve member banks					2,284 nonmember banks	
		4,197 member banks	Central reserve city			273 reserve city		3,892 country
			32 central reserve city	18 New York City	14 Chicago			
Public securities:								
Marketable.....	58,925	51,555	10,190	7,594	2,596	20,780	7,370	
Nonmarketable 2/.....	1,014 3/	702	21	15	6	114	237	
Total public securities.....	<u>59,940</u>	<u>52,257</u>	<u>10,211</u>	<u>7,609</u>	<u>2,602</u>	<u>20,894</u>	<u>7,607</u>	

Footnotes at end of Section II.

Table 2.- Summary of Public Marketable Securities

(Par values - in millions of dollars)

Classification	Held by 6,481 commercial banks 1/	Federal Reserve member banks					273 reserve city	3,892 country	2,284 nonmember banks
		4,197 member banks	Central reserve city						
			32 central reserve city	18 New York City	14 Chicago				
Type of security:									
Issued by U. S. Government:									
Treasury bills.....	5,194	4,275	913	679	233	1,312	2,050	919	
Certificates of indebtedness.....	6,686	5,935	1,470	1,107	363	2,382	2,083	750	
Treasury notes.....	12,285	10,760	2,139	1,613	526	4,524	4,097	1,525	
Treasury bonds.....	34,743	30,575	5,667	4,193	1,474	12,556	12,352	4,167	
Panama Canal bonds.....	11	3	1	1	-	2	*	7	
Guaranteed by U. S. Government.....	7	7	*	*	-	4	2	*	
Total.....	58,925	51,555	10,190	7,594	2,596	20,780	20,585	7,370	
Call classes:									
Due or first becoming callable:									
Within 1 year.....	18,254	15,849	3,722	2,847	875	5,830	6,297	2,406	
1 to 5 years.....	28,550	25,092	4,639	3,381	1,259	10,771	9,682	3,458	
5 to 10 years.....	11,410	10,023	1,706	1,264	442	3,989	4,329	1,386	
10 to 15 years.....	122	96	*	*	*	32	64	26	
15 to 20 years.....	130	100	7	6	*	34	59	31	
20 years and over.....	451	388	117	97	20	120	151	62	
Various (Federal Housing Administration debentures).....	7	7	*	*	-	4	2	*	
Total.....	58,925	51,555	10,190	7,594	2,596	20,780	20,585	7,370	
Tax status: 4/									
Wholly exempt from Federal income taxes....	11	3	1	1	-	2	*	7	
Partially exempt from Federal income taxes..	1,310	1,210	441	142	299	449	320	101	
Subject to Federal income taxes 3/.....	57,605	50,343	9,749	7,451	2,297	20,329	20,265	7,262	
Total.....	58,925	51,555	10,190	7,594	2,596	20,780	20,585	7,370	

Footnotes at end of Section II.

Section I.- Interest-Bearing Securities Issued or Guaranteed by the United States Government
Table 3.- Public Marketable Securities by Issues

(Par values - in millions of dollars)

Issue (Tax status $\frac{1}{2}$ is shown in parentheses)	Held by 6,481 commercial banks $\frac{1}{2}$	Federal Reserve member banks						2,284 nonmember banks
		4,197 member banks	Central reserve city			273 reserve city	3,892 country	
			32 central reserve city	18 New York City	14 Chicago			
Treasury bills:								
Regular weekly.....(taxable)	3,466	2,808	619	458	161	797	1,393	658
Tax anticipation.....(taxable)	1,051	924	259	200	60	334	331	126
Other.....(taxable)	678	542	35	22	13	181	327	135
Total Treasury bills.....	5,194	4,275	913	679	233	1,312	2,050	919
Certificates of indebtedness:								
2-1/2% February 1959-A.....(taxable)	1,279	1,118	210	159	51	470	438	161
1-1/2 March 1959-D $\frac{6}{10}$.....(taxable)	1,889	1,782	728	635	94	649	405	106
1-1/4 May 1959-B.....(taxable)	420	353	28	11	16	168	157	67
1-5/8 August 1959-C.....(taxable)	2,375	2,077	422	237	185	883	773	297
3-3/8 November 1959-E.....(taxable)	723	605	83	66	16	212	310	118
Total certificates of indebtedness.....	6,686	5,935	1,470	1,107	363	2,382	2,083	750
Treasury notes:								
1-7/8% February 1959-A.....(taxable)	2,063	1,851	465	385	80	768	618	212
3-1/2 November 1959-B.....(taxable)	369	302	50	26	23	70	182	66
3-1/2 May 1960-A.....(taxable)	1,058	888	82	50	32	410	396	170
3-5/8 May 1961-B.....(taxable)	582	472	92	36	56	139	241	111
$\frac{1}{2}$ August 1961-A.....(taxable)	1,091	889	81	57	24	356	452	202
3-5/8 February 1962-A.....(taxable)	170	142	6	1	5	57	79	28
$\frac{1}{2}$ August 1962-B.....(taxable)	1,292	1,108	148	108	40	547	413	183
3-3/4 November 1962-C.....(taxable)	699	592	88	61	27	290	214	107
2-5/8 February 1963-A.....(taxable)	3,191	2,953	833	627	207	1,258	862	238
1-1/2 April 1959-EA.....(taxable)	31	21	1	*	*	4	16	10
1-1/2 October 1959-BD.....(taxable)	38	29	7	*	7	5	16	9
1-1/2 April 1960-EA.....(taxable)	95	80	15	15	*	30	35	15

1-1/2	October	1960-EO.....(taxable)	149	118	24	13	12	34	60	31
1-1/2	April	1961-EA.....(taxable)	102	68	13	13	*	27	28	34
1-1/2	October	1961-EO.....(taxable)	203	178	25	24	1	82	70	25
1-1/2	April	1962-EA.....(taxable)	344	324	35	34	1	143	146	19
1-1/2	October	1962-EO.....(taxable)	427	392	60	56	5	188	144	35
1-1/2	April	1963-EA.....(taxable)	335	311	95	90	5	111	104	24
1-1/2	October	1963-EO.....(taxable)	46	42	18	18	*	5	19	4
Total Treasury notes.....			<u>12,285</u>	<u>10,760</u>	<u>2,139</u>	<u>1,613</u>	<u>526</u>	<u>4,524</u>	<u>4,097</u>	<u>1,525</u>
Treasury bonds:										
2-1/4%	June	1959-62.....(taxable)	2,538	2,249	465	415	50	904	880	289
2-1/4	December	1959-62.....(taxable)	1,336	1,187	351	233	118	385	451	149
2-1/8	November	1960.....(taxable)	2,663	2,354	329	257	71	1,141	885	309
2-3/4	December	1960-65.....(partially)	1,310	1,210	441	142	299	449	320	101
2-3/4	September	1961.....(taxable)	1,315	1,146	128	65	63	484	535	169
2-1/2	November	1961.....(taxable)	7,469	6,614	1,375	1,129	246	2,795	2,444	855
2-1/2	June	1962-67.....(taxable)	764	642	63	46	17	306	272	123
2-1/2	August	1963.....(taxable)	4,579	4,003	631	488	143	1,661	1,711	576
2-1/2	December	1963-68.....(taxable)	654	563	55	51	4	257	252	91
3	February	1964.....(taxable)	2,786	2,426	369	256	113	1,012	1,045	360
2-1/2	June	1964-69.....(taxable)	779	673	148	145	3	231	294	106
2-1/2	December	1964-69.....(taxable)	766	692	195	184	11	264	233	74
2-5/8	February	1965.....(taxable)	4,014	3,577	715	443	272	1,563	1,299	437
2-1/2	March	1965-70.....(taxable)	487	426	85	84	*	129	211	61
2-1/2	March	1966-71.....(taxable)	198	168	5	5	*	82	82	29
3	August	1966.....(taxable)	905	811	130	99	31	333	348	94
2-1/2	June	1967-72.....(taxable)	108	86	*	*	*	15	70	23
2-1/2	September	1967-72.....(taxable)	1,220	1,058	55	44	11	340	663	161
2-1/2	December	1967-72.....(taxable)	148	107	3	3	1	21	83	41
4	October	1969.....(taxable)	122	96	*	*	*	32	64	26
3-7/8	November	1974.....(taxable)	78	53	6	6	*	19	28	25
3-1/4	June	1978-83.....(taxable)	53	47	*	*	*	15	32	6
3-1/4	May	1985.....(taxable)	198	170	41	30	11	61	68	28
3-1/2	February	1990.....(taxable)	174	157	72	64	8	33	51	18
3	February	1995.....(taxable)	79	62	4	2	2	26	32	17
Total Treasury bonds.....			<u>34,743</u>	<u>30,575</u>	<u>5,667</u>	<u>4,193</u>	<u>1,474</u>	<u>12,556</u>	<u>12,352</u>	<u>4,167</u>

Footnotes at end of Section II.

(Continued on following page)

Section I.- Interest-Bearing Securities Issued or Guaranteed by the United States Government
Table 3.- Public Marketable Securities by Issues - (Continued)

(Par values - in millions of dollars)

Issue (Tax status <u>4/</u> is shown in parentheses)	Held by 6,481 commercial banks <u>1/</u>	Federal Reserve member banks					2,284 nonmember banks	
		4,197 member banks	Central reserve city			273 reserve city		3,892 country
			32 central reserve city	18 New York City	14 Chicago			
<u>Panama Canal bonds..... (wholly)</u>	<u>11</u>	<u>3</u>	<u>1</u>	<u>1</u>	<u>-</u>	<u>2</u>	<u>*</u>	<u>7</u>
<u>Guaranteed securities:</u>								
Federal Housing Administration debentures.....(taxable <u>7/</u>)	<u>7</u>	<u>7</u>	<u>*</u>	<u>*</u>	<u>-</u>	<u>4</u>	<u>2</u>	<u>*</u>
<u>Total public marketable securities.....</u>	<u>58,925</u>	<u>51,555</u>	<u>10,190</u>	<u>7,594</u>	<u>2,596</u>	<u>20,780</u>	<u>20,585</u>	<u>7,370</u>

Footnotes at end of Section II.

Table 4.- Public Nonmarketable Securities by Issues

(Par values - in millions of dollars)

Issue (Tax status $\frac{1}{2}$ is shown in parentheses)	Held by 6,481 commercial banks $\frac{1}{2}$	Federal Reserve member banks					2,284 nonmember banks	
		4,197 member banks	Central reserve city			273 reserve city		3,892 country
			32 central reserve city	18 New York City	14 Chicago			
United States savings bonds:								
Series F $\frac{2}{2}$.....(taxable)	178	111	1	-	1	8	102	67
Series G.....(taxable)	355	268	1	1	1	29	238	87
Series J $\frac{2}{2}$.....(taxable)	*	-	-	-	-	-	-	*
Series K.....(taxable)	2	1	-	-	-	*	1	1
Total United States savings bonds.....	535	380	2	1	2	37	341	155
Other U. S. securities:								
Depository bonds.....(taxable)	203 $\frac{3}{3}$	110	11	11	-	24	75	18
Treasury bonds:								
Investment Series A.....(taxable)	145	113	7	3	4	37	68	33
Investment Series B.....(taxable)	130	99	1	-	1	16	83	31
Total other U. S. securities.....	479 $\frac{3}{3}$	322	19	15	5	77	226	82
Total public nonmarketable securities.....	1,014 $\frac{3}{3}$	702	21	15	6	114	567	237

Footnotes at end of Section II.

**Section II. - Interest-Bearing Securities Issued by Federal Agencies but
Not Guaranteed by the United States Government**

(Par value - in millions of dollars)

Issue (Tax status $\frac{4}{1}$ is shown in parentheses)	Held by 6,481 commercial banks $\frac{1}{1}$	Federal Reserve member banks					2,284 nonmember banks	
		4,197 member banks	Central reserve city			273 reserve city		3,892 country
			32 central reserve city	18 New York City	14 Chicago			
Banks for cooperatives:								
1.70% March 1959 (Debentures)..(taxable)	21	18	*	*	*	10	7	4
2.85 April 1959 (Debentures)..(taxable)	27	19	1	*	1	6	12	8
3-1/2 June 1959 (Debentures)..(taxable)	23	18	*	*	*	4	14	6
Total banks for cooperatives securities.....	71	54	2	*	1	20	33	17
Federal home loan banks: 8/								
1-1/4 January 1959 (Notes).....(taxable)	20	16	2	*	1	7	8	4
1.60 February 1959 (Notes).....(taxable)	35	25	3	3	*	8	14	9
3-1/4 March 1959 (Notes).....(taxable)	38	26	1	1	*	5	21	12
3-1/2 April 1959 (Notes).....(taxable)	24	16	*	*	*	3	13	8
3-1/8 April 1963 (Bonds).....(taxable)	94	76	1	-	1	53	22	18
Total Federal home loan bank securities.....	211	160	7	4	3	76	78	51
Federal intermediate credit banks:								
Debentures.....(taxable)	347	278	20	14	7	111	147	68
Federal land banks: 9/								
4-5/8 February 1959 (Bonds)....(taxable)	40	32	3	*	3	8	21	8
2-1/4 May 1959 (Bonds)....(taxable)	31	25	1	1	1	11	13	6
3-1/2 May 1959 (Bonds)....(taxable)	37	28	*	*	*	9	20	8
1-3/4 October 1959 (Bonds)....(taxable)	73	63	2	1	1	30	31	11
2-1/4 February 1960 (Bonds)....(taxable)	68	57	7	2	5	23	28	10
2-1/2 June 1960 (Bonds)....(taxable)	51	41	1	*	1	14	26	10

3-3/8	April	1961	(Bonds)....(taxable)	35	27	1	1	*	9	17	9
4	September	1961	(Bonds)....(taxable)	42	30	*	*	*	7	23	12
4	May	1962	(Bonds)....(taxable)	20	15	*	-	*	3	11	5
2-3/4	May	1963	(Bonds)....(taxable)	73	59	2	*	2	31	26	15
3-1/4	May	1966	(Bonds)....(taxable)	40	30	1	*	1	13	16	10
4-1/8	February	1967-72	(Bonds)....(taxable)	3	2	*	*	*	1	1	1
4-1/2	October	1967-70	(Bonds)....(taxable)	4	3	*	*	*	*	3	1
4-5/8	July	1969	(Bonds)....(taxable)	2	2	*	*	*	*	2	*
3-1/2	April	1970	(Bonds)....(taxable)	9	6	*	*	*	2	4	3
3-1/2	May	1971	(Bonds)....(taxable)	1	*	-	-	-	*	*	*
3-7/8	September	1972	(Bonds)....(taxable)	*	*	*	*	*	*	*	*
Total Federal land bank securities.....				<u>529</u>	<u>421</u>	<u>19</u>	<u>7</u>	<u>12</u>	<u>160</u>	<u>242</u>	<u>108</u>
Federal National Mortgage Association:											
3%	February	1959	(Debentures)....(taxable)	35	28	*	*	*	5	22	7
1.65	April	1959	(Debentures)....(taxable)	33	27	1	1	*	11	14	6
2	June	1959	(Debentures)....(taxable)	32	26	1	*	1	11	14	6
3-7/8	August	1959	(Debentures)....(taxable)	29	22	5	5	*	2	14	7
3-5/8	August	1960	(Notes).....(taxable)	460	403	135	103	32	125	144	57
3-1/2	February	1962	(Debentures)....(taxable)	65	47	3	1	2	15	30	18
3-1/4	March	1963	(Debentures)....(taxable)	58	42	1	*	1	19	22	16
4-1/8	November	1963	(Debentures)....(taxable)	21	13	1	1	*	2	10	8
4-3/8	June	1965	(Debentures)....(taxable)	31	23	8	8	*	2	13	7
3-5/8	March	1968	(Debentures)....(taxable)	19	15	4	4	1	6	4	4
Total Federal National Mortgage Association securities.....				<u>782</u>	<u>646</u>	<u>159</u>	<u>122</u>	<u>37</u>	<u>199</u>	<u>288</u>	<u>136</u>

- 1/ Includes trust companies and stock savings banks but excludes securities held in trust departments.
- 2/ United States savings bonds, Series F and J, are shown at current redemption value. They were reported at maturity value by the banks included in the Treasury Survey but have been adjusted to current redemption value for use in this statement.
- 3/ Total includes \$75 million depository bonds held by commercial banks not included in the Treasury Survey.
- 4/ Federal securities fall into three broad classes with respect to the imposition of Federal income taxes on income derived from them. "Wholly" tax-exempt securities are those with the income exempt from both normal tax and surtax. "Partially" tax-exempt securities are those with the income exempt from the normal tax except that in the case of partially tax-exempt Treasury bonds, interest derived from \$5,000 of principal

- amount owned by any one holder is also exempt from the surtax. "Taxable" securities are those with the income subject to both normal tax and surtax.
- 5/ Includes Federal Housing Administration debentures; see footnote 7.
- 6/ Tax anticipation series.
- 7/ A small indeterminate amount of these debentures is partially tax-exempt.
- 8/ The proprietary interest of the United States in these banks ended in July 1951.
- 9/ The proprietary interest of the United States in these banks ended in June 1947.
- * Less than \$500,000.

Representative PATMAN. Also, Mr. Secretary, I believe it would be helpful to have some factual information concerning the percentage of securities which have been purchased from the Treasury by the biggest purchasers of securities.

Would you please supply for this record later a list of each of the 50 biggest purchasers of securities from the Treasury over the past 2 years in each of the categories listed below. Then, if you would show the total amount of each issue which each of these companies offered to subscribe, and the amount they were actually sold plus also the combined totals for each category, this would be very helpful. In other words, to illustrate with commercial banks, I would like to know the amount that all commercial banks in the country offered to subscribe to each issue, the amount of the allotments to all commercial banks, and then I would like to have the same information for each of the 50 largest commercial banks.

The other types of institutions for which I would like to see similar information are: individuals, insurance companies, mutual savings banks, utility corporations, all other corporations, private pension and retirement funds, State and local governments, dealers and brokers, and others.

(At the time the hearings were printed the problem involved in supplying the requested data was still under examination. If and when the data is supplied, it will be published in a later part of these hearings.)

In your report that you made with Chairman Martin I notice that you did not say anything about the enormous profits made by a few banks in 1958, obviously by reason of a depression in Government bonds in 1957. Did you cover that in your investigation, Mr. Secretary?

Secretary ANDERSON. We did not get into the profit question.

Representative PATMAN. You know, I am sure, that in 1958 the banks made 10 times as much as they did the year before, speculating on Government securities. In fact, they made the enormous amount of \$681 million.

No doubt all banks did not make money but the 20 largest banks made over \$220 million and the banks of over \$500 million of deposits made about \$300 million.

I just wonder why you did not look into that.

Secretary ANDERSON. Congressman Patman, it has long been the policy of the Treasury, long before I came to it, that all subscribers of Government securities are treated alike.

Representative PATMAN. We are not talking about subscribers here, Mr. Secretary. We are talking about speculating in Government bonds in an unregulated, unsupervised market.

Representative CURTIS. Will the gentleman yield just for a moment?

Representative PATMAN. I would be glad to.

Representative CURTIS. In regard to your testimony, I wonder if you would supply for the record the source of your material?

Representative PATMAN. Certainly. I would be very glad to. It is the very best. (See p. 1183.)

Representative CURTIS. I am sure it is.

Secretary ANDERSON. I wanted to make these points.

Subscriptions, as you know, come to the Treasury through the Federal Reserve Banks over the country.

Representative PATMAN. Mr. Secretary, I reiterate that I am not talking about issues that are subscribed. I am talking about buying and selling Government bonds in a speculative market.

Secretary ANDERSON. You mean as between themselves?

Representative PATMAN. Yes, and all the other people of the country including corporations. I am not talking about your dealing in selling issues. They could not have made that much money in the sale of your issues. They made \$681 million in 1 year. That does not include the interest they made on those bonds. That is just the appreciation that they made.

The only year in which there was the least comparison was after the 1953 depression. The banks made \$421 million in 1954 the same way. It is beginning to look like a pattern, Mr. Secretary.

You have a recession in 1953. They make \$421 million the next year in profits on the sale of your securities. Then we have a big dip in 1957 and bonds go up in 1958 and the banks make \$681 million. Now it looks as if they are expecting to make it in 1960. It looks like they are shortening these cycles.

I was just hoping that the Treasury and the Federal Reserve would go into that.

Secretary ANDERSON. Congressman, I think when you see the material, there is a considerable amount of effort devoted to the problems of limiting speculation.

When we get into such things as what happened in the 50 large subscribers or holders of securities, we have for many years in the Treasury had regulations under which we have operated—not just in my administration, but others—in which the portfolio holdings of various owners of Government securities from time to time were obtained only on a very confidential basis. They are not even examined by the policymaking individuals of the Treasury. These are held by the people who over the years remain permanent employees of the Treasury.

By classes of investors of various kinds, this information is always available to us, and we will make it available to the Congress.

Representative PATMAN. I am not insisting on your going into individual corporations or banks. It occurs to me that the very fact that they can make \$681 million in 1 year, which is 10 times as much as they made the year before, is enough to excite inquiry; in fact, suspicion. It is a very large amount of money in proportion to the resources of the banks.

Secretary ANDERSON. I think, from the standpoint of the examination which we have made, it was not on the question of the profitmaking but, rather, on the question of what kind of procedures might be considered in order to minimize the speculation in the market regardless of whether that speculation resulted in profit or in loss.

When you come down to a question of the profits of banks, in a period of recession such as we had last year, the prices of securities rise. Whereas in the past they may have been selling below par, they go above par. There are profits which are realized in the trade, in exchange and sale of those Government securities during that year. They would be nonrecurring gains, as you have indicated, rather than gains that result from interest rates.

It also would have to be examined in the context of the fact that some of those very institutions which were able to show profits last year because of the high price of Government securities, will this year be showing comparative losses because of the decline in Government securities.

Representative PATMAN. With all due respect to the Secretary, I know he is sincerely trying to answer the question, but I do not think his answer is responsive to my question.

Secretary ANDERSON. I am sorry.

Representative PATMAN. There are only 17 dealers between the Government and the money markets. Did not that excite your interest and did it not cause any suspicion in your mind about the possibility of its being too tight a market there for 17 dealers?

Secretary ANDERSON. You will find in the data that considerable inquiry was made into why there are not more; why, for example, more people who are dealing in the stock market do not deal more in Government securities than in corporate securities.

Representative PATMAN. I am not talking about that.

Secretary ANDERSON. Why there are not more dealers?

Representative PATMAN. I am speaking about the Government bond market, unsupported, unregulated with only 17 dealers having the privilege of dealing with these securities.

Did you notice any particular number of these dealers having an inside line into the operations of the market in a way that would excite your attention or suspicion that they are so closely connected with the Government securities market that they would be in a position to get inside information?

Secretary ANDERSON. I must say to the Congressman that I have not examined all of the factual material because it is just coming out today. I have up to now seen nothing that would make me think they had inside information.

Representative PATMAN. Because these dealers would be so closely in touch with the Federal Reserve Bank of New York where the account is and where all these Government trades are made, and that they are on boards that help select them—the people who are running the show up there—do you think there is any probability of inside knowledge or information that would allow these people to enrich themselves unduly because of that knowledge?

Secretary ANDERSON. I do not have any information of that kind, Mr. Congressman.

Representative PATMAN. You do not have any reason to believe that anything like that is going on?

Secretary ANDERSON. Not at this moment; no, sir.

Representative PATMAN. And you did not receive any information that would excite your curiosity?

Secretary ANDERSON. When you ask did I receive, this work has been done up to now by the study group, and I must be frank to say that the details of all of the study I have not yet read. But, as of now, I have no reason to believe any such operations have taken place.

Representative PATMAN. If one of these dealers happens to have enriched itself in what could properly be termed undue proportion to profits of past years, and that one particular dealer had close and

intimate contacts with the people who handle that market, would that not probably excite your suspicion?

Secretary ANDERSON. It would be the sort of thing that we would want to examine as a matter of policy.

When one looks at profits and losses, if you take the period from 1955 to 1958, profits on securities ran about \$830-odd million. If you look at the losses on securities in the same period, they were about \$870 million.

Representative PATMAN. Yes, sir.

I have time for one more question, I think.

Has the Federal Reserve properly and adequately given you the assistance and cooperation that you believe you are entitled to as Secretary of the Treasury?

Secretary ANDERSON. Congressman, I would say that any time that there are agencies of Government, each independent of the other and, yet, instances where they have responsibilities that affect areas that overlap, there is bound to be from time to time some measure of difference in judgment as to the time and way in which all of the operations operate.

I think that, if I may take the liberty of referring to a comment which the distinguished chairman made some years ago, he used what I think was a very good analogy in saying that "good fences make good neighbors."

The CHAIRMAN. That was taken from a poem by Robert Frost.

Secretary ANDERSON. I was attributing it to the chairman. What we do is to try to exchange information as best we can. The mechanics are something like this: I have the chairman of the Federal Reserve Board to lunch on each Monday to talk over and exchange information. The staff of the Federal Reserve and the Treasury meet in the Federal Reserve on Wednesday at lunch and thereafter exchange information. The staff people are continually working with each other.

Since my coming here, as you know, the President has met on an informal basis from time to time with the Chairman of the Federal Reserve Board, myself, the Chairman of the Council of Economic Advisers, the Economic Adviser to the President, in which there is a free and uninhibited exchange of information and ideas.

While each of us makes his decision and has his responsibilities for the various fields in which we operate, we do try to exchange information so that the judgments which are going to be made by the respective bodies are at least made in the light of and with the knowledge of problems, information, and judgments concerning the others.

Representative PATMAN. Has the Federal Reserve assisted you in lowering interest rates or trying to lower interest rates?

Secretary ANDERSON. I would not say that as a deliberate policy we have ever asked the Federal Reserve Board to try to fix or to move an interest rate up or down.

Representative PATMAN. Thank you, sir. My time has expired.

The CHAIRMAN. Senator Bush?

Senator BUSH. Mr. Chairman, I would like to ask Congressman Patman, before he leaves, about those figures he brought into the record about the bank profits.

Did you mention \$800 million or thereabouts as trading profits?

Representative PATMAN. \$681 million.

Senator BUSH. And those were the so-called capital gains from trading?

Representative PATMAN. Yes, sir.

Senator BUSH. From how many banks?

Representative PATMAN. All banks were involved in the aggregate.

Senator BUSH. All banks in the country, 14,000 banks?

Representative PATMAN. 13,000 banks. But the 50 largest banks profited to the extent of 44.6 percent of that total amount.

Senator BUSH. Do your figures tell us on how big a volume of trading this occurred?

Representative PATMAN. No; it does not.

Senator BUSH. Was it \$2 billion or \$200 billion? Have you any idea?

Representative PATMAN. No; I only put the aggregate profits of \$681 million down, and had them written down as to the beneficiaries of the profits.

Senator BUSH. I would say that with all respect to the gentleman from Texas, I do not think the figure is very significant if you do not relate it to a total volume of trading?

Representative PATMAN. I related it to the 50 banks that made about \$300 million in 1 year. That is pretty good.

Senator BUSH. Of course, you do not relate it even to the assets of those banks, their holdings of Government bonds, or anything else?

Representative PATMAN. That is right.

Senator BUSH. This, I think, makes it a completely irrelevant figure.

I would say unless you can furnish us with some figures we can relate that to, we can hardly be impressed with that.

Representative PATMAN. They do this on a very low margin of sometimes 5 percent or even less.

Senator BUSH. Mr. Chairman, so much for that.

I think the chairman has given us a good exhibit in connection with the joint participation of the Federal Government in the bond markets and how it relates to the State and local governments and corporations. It shows that, any way you look at it, the Federal Government is a very important factor in the overall market, even if you rule out refunding and simply look at the money involved in new issues.

On that basis, if I see this correctly, the Federal Government would amount to about 30 percent, anyway. So it is a very big factor.

It is a much larger factor, is it not, Mr. Secretary, when the Government has to raise new money, than when its operations are confined to refunding?

Secretary ANDERSON. That is correct, sir.

Senator BUSH. That, of course, has been the case in the last year?

Secretary ANDERSON. Yes, we have been raising more money because of the deficit.

Senator BUSH. Yes.

Conversely, if we had a surplus in the Government budget, that would seem to reduce the influence of the Government in the total bond market, because it would be a buyer of bonds rather than a seller. Is that not true?

Secretary ANDERSON. I think a good period to relate your question to is the period of 1921 to 1929, when the Federal debt was reduced by one-third in a period of relatively increasing levels of activity, and in which the cost of money at the interest rate tended downward, because we were a net supplier of funds.

Senator BUSH. So, as you emphasize in the closing part of your statement, the problems of fiscal imbalance during prosperous times have a tremendous effect on the whole question of growth and stability.

But they also have a real direct effect on the Government bond market; is that not true?

Secretary ANDERSON. That is correct.

Senator BUSH. I bring this out to show that one of the real problems in connection with the Government bond market is the Government deficit, and the way to cure that is to create a surplus rather than to continue to operate at a deficit. Doing that would tend to take the pressure off of interest rates and tend toward bringing about lower interest rates. Is that not true, Mr. Secretary?

Secretary ANDERSON. I think so, sir.

The CHAIRMAN. Would you yield?

Senator BUSH. I would love to yield to my distinguished chairman.

The CHAIRMAN. This eloquent statement about Government surplus would seem to indicate you join the Senator from Illinois in closing those loopholes?

Senator BUSH. I would certainly join the Senator from Illinois in his major objective. I do not know what loopholes he is referring to.

The CHAIRMAN. The loopholes against which the Senator from Connecticut voted—in part.

Senator BUSH. That, of course, is the Senator's private definition of loopholes. Everybody has his own definition of that.

The CHAIRMAN. Excuse me, Senator. I will give you extra time.

Senator BUSH. That is very generous of you. I do not think I will need it.

This leads me, then, Mr. Secretary, to another question. Inasmuch as the Federal Government is a large factor in the market, it seems to me that it should have as much freedom as possible with offering securities that are attractive to the market, which leads me to the issue that is pending before the House of Representatives at the present time with respect to the interest ceiling on long-term Government bonds.

I ask you if it would not assist the Treasury materially and promptly in dealing with this very heavy burden of responsibility of financing this enormous Government debt, if the interest ceiling were eliminated?

Secretary ANDERSON. Yes, I think so, sir.

Senator BUSH. Another point.

It has been suggested from time to time that the market in Government bonds would be facilitated by the Federal Reserve buying long-term bonds. It has always seemed to me, frankly, that that is just as inappropriate as it would be for the commercial banks having demand deposits to buy long-term bonds. I do not think they would long hold the confidence of the depositors if that became a general practice, of increasing demand deposits in long-term bonds. But

there are those who believe that the Federal Reserve should be doing that very thing with its demand deposits.

Would you care to comment on that particular suggestion that has been made concerning Federal Reserve policy?

Secretary ANDERSON. The whole problem is this. There is a market for certain securities in our country of different kinds and characteristics because of the different needs of institutions. Some institutions buy long-term bonds because they have amortization requirements; they are interested in getting a security that will meet their amortization requirements, and simply holding it over the years, regardless of fluctuations that may take place in the price of the bond. We have today about \$78 billion of debt which is due within a year, and as we look forward to the next 18 months, we will have close to \$100 billion coming due within a year if we do nothing except roll over in 1-year securities.

Then, if we look also at the problem of the seasonal fluctuations, which run \$5 or \$6 billion, there would be times when we would run considerably over \$100 billion which is due within a year if we issued nothing over a year.

Again, just as we have some people who want long-term securities in this country, we have a certain amount of liquidity requirements. I think there might be differences of judgment as to just how much those liquidity requirements are. But if you oversupply the liquidity requirements and put money into the short-term sector, then, of course, you tend to push up the short-term rate.

If the Federal Reserve initiates a practice of buying long-term bonds and then selling short-term issues, you have to assess the fact that in selling the short-term securities to offset the purchase of the long-term securities, you would be putting additional pressure on the same short market which is already under pressure because of the heavy Treasury financing in that area.

If you did not offset the sale of the long-term bonds by selling short-term bonds, you would simply have added to the money supply. If you added to this money supply by buying long-term securities or any other kind of securities without an offsetting transaction, then you are supplying into the market what we call high-powered money. This money will be used by the banking system as additional reserves, and the amount of money put into the market has an expansive capacity of about five or six times. If this expansive capacity takes place at a time when the level of business is already high, then you tend to create inflationary pressures. If you create inflationary pressures, the borrower becomes unwilling to lend unless at a higher price, because he thinks the future value of his money will be eroded and the borrower becomes willing to pay higher interest rates because he thinks he will pay off the loan with cheaper dollars than he is borrowing now. So the interest cost or the cost of money would tend to rise.

One must also examine the kinds of people who deal in these various markets. For example, let us say, who uses the 1-year money in our country? This is normally the fellow who pays his bills at the end of the month on the installment plan. It is the fellow who accumulates some money for taxes, whether they are income taxes or other taxes, the man who borrows to meet his payrolls. The fellow who borrows

normally in the 1- to 5-year cycle is the man who borrows for working capital purposes or for such things as financing durables like automobiles, household goods, that sort of thing. As these rise and there is this pressure, the cost of money in this sector tends to go up.

So it would seem to me that what we ought to do is to have the flexibility of not having the Government confined by statute within the area of 1 to 5 years, but of giving the Government the capacity to finance more soundly and extend some of the debt beyond that point.

I ought to be clear by saying that even if we were given this authority, we would use it with discretion. We would certainly not try to go into long-term markets indiscriminately. We would consider the rates which we would have to pay, and we would also consider requirements of other institutions and other segments of business. But I think it would go a great way in relieving the pressure on the short-term market.

Senator BUSH. Mr. Chairman, I would just like to associate myself with the complimentary remarks of Mr. Curtis regarding Secretary Anderson's opening statement. I think it is an excellent statement and will be very helpful to the committee.

The CHAIRMAN. Congressman Reuss?

Representative REUSS. Thank you, Mr. Chairman.

Mr. Secretary, I have been listening with interest to your colloquy with Senator Bush just now. Now I would like to ask you about something that I gather you were not discussing. I would like to ask you specifically about the bill reported out by the House Ways and Means Committee a couple of weeks ago which first lifted the 4 $\frac{1}{4}$ -percent ceiling for a couple of years and then expressed the sense of Congress that the Federal Reserve, when it was engaged in its good judgment in increasing the money supply, should do so by the method of purchasing U.S. securities of varying maturity.

I read in the New York Times this morning that the Treasury, which appeared to accept the sense-of-Congress amendment at first, has now made plain its opposition. Would you make plain to me your opposition, first by telling me whether you support or oppose the sense-of-Congress amendment which I just placed before you?

Representative CURTIS. Would the gentleman yield?

Representative REUSS. Not at this moment.

Representative CURTIS. Just for correction.

Representative REUSS. Not at this moment. I will presently.

Secretary ANDERSON. Congressman Reuss, may I say, without any intent of evading any part of your question, that this bill is not yet reported out of the House Ways and Means Committee. I have been advised there will be other discussions, in all probability.

Representative REUSS. However, will you give me your views on it? I know you are thoroughly familiar with it. And would you tell me whether you favor that language or oppose it? Just yes or no is all I need on that. Then I want to ask your reasons.

Secretary ANDERSON. I frankly would not like to give a yes or no answer. I would like to give an expository answer, if I may.

Representative REUSS. Then I gather you do not oppose it?

Secretary ANDERSON. I would not say I did not oppose it, no, sir. May I have just a moment?

Representative REUSS. Before you go into the expository answer, is it correct you are unable to say whether you favor or oppose the sense-of-Congress resolution which I have just put before you?

Secretary ANDERSON. I will say that so long as it is pending before the House Ways and Means Committee, it is proper that I should make no final declaration except to that committee.

Representative REUSS. Do it to me, because I wrote the amendment, it has been sent to you, and you have been talking to the press about it—perfectly properly, I think. I just want to be let in on it.

Secretary ANDERSON. At the time when the amendment was proposed, we made quite clear, I thought, that we in the Treasury must be concerned not only with what the words themselves said, and not only with the interpretation which the members of the committee and the Members of the Congress might place upon those words, but that we must be concerned as well about the public interpretation that might be placed upon it.

We are dealing here in an area of confidence. We are seeking to improve confidence in sound management of our fiscal affairs by getting a greater degree of flexibility in the management of the debt as per our original request.

I do not think that any of us are precisely wise enough to know how confidence is motivated, but I do believe that since the discussions have taken place with reference to the amendment, I have a growing concern that the portion of the amendment which relates to the suggestion that the Federal Reserve buy varying maturities, would tend to impair confidence generally.

Representative REUSS. May I interrupt right there to break down your various reasons.

I gather you do not object to the Congress, under its constitutional power to coin money and regulate the value thereof, giving appropriate direction to the Federal Reserve, as a matter of principle?

Secretary ANDERSON. I do not as a matter of principle object to any general instructions which the Congress would want to give to the Federal Reserve. I must be frank to say I would hope that any such general instructions should be given in the context of amending the Federal Reserve Act rather than in the context of amending a debt management law.

Representative REUSS. Let me next ask, do you object to anything in that sense-of-Congress amendment other than three words "of varying maturity"? Specifically, do you object to the congressional direction to the Federal Reserve System that when, in its judgment, it is in the act of increasing the money supply, it should do so for the life of the Ways and Means Committee amendment, 2 years, by purchasing U.S. securities? Bear in mind that bills are a U.S. security and that that part of the language could be satisfied by purchasing bills. Do you object to that?

Secretary ANDERSON. Congressman Reuss, it is my own judgment that the Congress can give any kind of general instructions that it wants to, to the Federal Reserve.

Representative REUSS. But my question was, is this particular instruction one that you favor or oppose?

Secretary ANDERSON. I think it is wise for the Congress to limit its suggestion in terms of objectives and in terms of policies and not

in terms of saying that these are the detailed ways in which those objectives might be reached.

Representative REUSS. Well, this is a bill that goes beyond details, Mr. Secretary. This suggestion of the Ways and Means Committee, in which I heartily join, is that instead of lowering bank reserves, the Federal Reserve for the life of the resolution, 2 years, shall add to the monetary supply, when it deems it should be added to, by buying U.S. securities. I believe that that helps the taxpayers, it prevents undue downward fluctuations of the securities bought, and it prevents attrition.

Do you disagree with that? And if so, what are your reasons, so that the public debate may be conducted in a more informed manner than it has so far.

Secretary ANDERSON. The longrun monetary needs of the United States are expected to grow. If one looks historically, they might be expected to grow at the rate of 3 percent or more, if that is the rate of our national growth.

The bank reserves that are necessary to this growth can be increased by increasing our gold stocks. It can be taken care of by expansion in the Federal Reserve holdings of Government securities. It can be increased or reduced by bank reserve requirement changes.

Representative REUSS. That is exactly right.

Now, the amendment says, for the next 2 years, to help in the debt management crisis, let us furnish needed additions to the money supply by purchase of U.S. securities.

Secretary ANDERSON. When you get to the question as to what extent the needed monetary growth should be supported by Federal Reserve purchases of securities as opposed to reduction in the reserve requirements, you have to weigh the fact that the pattern of development in postwar business cycles suggests strongly that monetary expansion should be restrained during periods of business expansion, in order to limit inflationary pressures.

Representative REUSS. Yes, we are all agreed on that. The point was simply this. When the Federal Reserve pursues the policy it has announced of raising the money supply by 3 percent per annum on the average, a policy which you have just reiterated, how should they do it?

Secretary ANDERSON. This is the point I am coming to.

In a recessionary period, it is desirable that you have as fast an increase in money supply as you can accomplish, and that this money supply be widely spread as quickly as you can. If you lower bank reserves all over the country at one time, the various banks immediately have more reserves against which there can be credit expansion, pushing the economy forward.

In times of high levels of business activity, if one proposed to decrease liquidity or reserves by the use of the technique of raising reserve requirements, then I think you would have distortions, in that you would have—

Representative REUSS. If I may interrupt, Mr. Secretary, we are not talking about decreasing reserves. We are talking about what happens when the Federal Reserve, in its own good judgment, decides that the money supply, i.e., bank reserves, should be expanded.

I say, and the Ways and Means Committee says, that this should be

done for the next 2 years by buying U.S. securities. You are opposed. I want to know why?

Secretary ANDERSON. What I am saying is that at this moment any suggestion that we increase bank reserves, it would seem to me, would be only to add to the inflationary problem.

Representative REUSS. Precisely. We are talking about the next 2 years, however. If the Federal Reserve does not deem it wise to increase reserves and the money supply, then that is fine. Then this resolution has no effect, because there is no increase. But the question to which I asked you to address yourself is, What if, within the next 2 years, the Federal Reserve says it is going to do what it has recently testified it is going to do at some point, namely, raise the money supply by 3 percent. I, and the Ways and Means Committee, want them to do that by buying the securities. You do not. Why?

Secretary ANDERSON. Here is what I am trying to say to you.

If the turnaround out of a period of high level of business activity into one of recession—if that is what brings it about, then I would say that I would not now want to prejudge. But my disposition is to say that you would probably want to get the reserves into the banks more rapidly than you would get them by purchasing securities. You would want to get them in faster by lowering reserve requirements.

Representative REUSS. There are \$63 billion worth of securities in the banks. Since a purchase of \$1 billion of those by the Federal Reserve permits an augmentation of the money supply on the order of 4 percent, that is, beyond the wildest dreams of the Federal Reserve, it does seem to me you are straining at gnats a bit there, Mr. Secretary.

Secretary ANDERSON. Let us assume that in 3 months from now, instead of going up, we turn sharply downward and it looks like that is going to continue for awhile. I would say that, not trying to prejudge, you might very well want to increase the reserves, not by buying Government securities but by lowering reserve requirements, or maybe by both.

On the other hand, let us assume that we have a continuing rise of activity over the whole 2 years and you want to increase the money supply, but only at a rate that is not going to add to inflationary pressures. Then I would think that increasing the money supply by buying Government securities would be the appropriate way of doing it.

Representative REUSS. Then, I gather that your sole objection to the part of the sense-of-Congress resolution which says when you expand the money supply, do it by buying securities, other than this metaphysical one about confidence, which I frankly do not understand, the sole objection to the resolution is that if there were a depression, and you needed to expand the monetary supply very fast, buying U.S. securities might not let you rush pell-mell into the monetary expansion which you wanted, fast enough. To that I would say, if that happens, I know Congress would be delighted on 24 hours' notice to give the administration the power to accelerate any expansion of the money supply.

This, however, does not seem to be the problem now.

Do I have time to yield to Mr. Curtis?

Representative CURTIS. The correction has already been made to the effect that the Ways and Means Committee has not reported out, and I am afraid the gentleman is under a misapprehension when he says the Ways and Means Committee agrees with him.

Representative REUSS. The majority do.

Representative CURTIS. Not even the majority. Six of us, and I was among them, who agreed to vote this bill out, which has not been voted out, did it only with the reservation that we would oppose your amendments on the floor. We are opposed to them, and the majority of the committee is opposed to your amendments.

Representative REUSS. Let us say a substantial and very intelligent, minority of the Ways and Means Committee, then.

The CHAIRMAN. Mr. Javits?

Senator JAVITS. Mr. Secretary, first I assume that when you give the information for Representative Patman you will also include the losses which may have been suffered in connection with the same general period of years, and that you will also give us some sense of the relationship, which Senator Bush has mentioned, between the resources which were engaged in, either losses or profits; and I hope, too, you will look into the question, if your attention has not been directed to it before, of the small number of dealers and any relationships which may exist between the dealers and the Federal Reserve banks, or any other agencies of the Government which deal with this question.

Secretary ANDERSON. Senator Javits, we will by classes be delighted to give you such information as we can on both sides.

(The material referred to is as follows:)

The questions on bank profits on securities relate to (1) calendar 1958 experience on both profits and losses, (2) relevance of 1 year's figures versus experience for a full business cycle, and (3) seeming concentration of profits in larger banks. Each will be taken up in turn.

1. *Calendar 1958 experience.*—During the calendar year 1958, banks realized a net gain on securities transactions of \$588 million, or a capital gain, in effect, of less than three-fourths of 1 percent of the \$81½ billion average securities holdings during the year (\$62¼ billion Governments plus \$19¼ billion municipalities and corporates).

(Data compiled by the Federal Reserve on the earnings of insured commercial banks in the United States indicate gross profits on securities (including State and local government and corporate securities as well as Federal securities) of \$682 million for the calendar year 1958, and gross losses on securities for the same year of \$94 million, for net profit of \$588 million.)

2. *Experience over a business cycle.*—Figures on bank profits on securities for a single year are very misleading, however. During the past 4 years, for example, bank security losses exceeded profits.

During a recessionary period, such as the first half of 1958, interest rates fall as the result of easier credit conditions and prices of outstanding securities in the market rise. In that environment banks show a profit on their securities transactions. However, during the high prosperity of 1955, 1956, and 1957, interest rates were rising and securities prices were declining. Commercial bank losses on securities transactions substantially exceeded gains, therefore, in each of those 3 years.

For the entire 4 years (corresponding very closely in time to one complete turn of the business cycle) bank profits on securities totaled \$834 million and losses in the same period totaled \$870 million, for a net loss from securities transactions of \$36 million for the 4-year period.

Net profits by banks on securities, calendar years 1955-58

[In millions of dollars]

	Gross profits	Gross losses	Net profits (+) or losses (-)
1955.....	57	221	-164
1956.....	31	317	-286
1957.....	64	238	-174
1958.....	682	94	+588
Total.....	834	870	-36

Over a period of time bank losses on sales of securities would tend to exceed profits since banks are typically forced to sell securities on net balance on a declining market as they meet mounting loan demands in the face of tightening credit conditions. Conversely, they buy most of their Governments, on net balance, when interest rates are declining and securities prices rising, since that is when loan demand is slack and money easier. Bank losses on securities are expected to exceed profits by a substantial margin again in 1959 on the basis of the declining prices in the market thus far.

Banks are, of course, permitted to carry Government securities on their books at cost if bought below par, regardless of their current market value. Nevertheless, it has been estimated that the market value of bank holdings of Governments has declined by about \$3½ billion during the past year so that losses could be substantial if holdings decline further, particularly in securities still several years or more from maturity. This potential loss, even though only a small part is ever realized, is an important restraint on too rapid an expansion of private bank credit, as well as a source of concern to every bank as it tries to meet the needs of its customers. (There was an increase of about \$2¼ billion in the market value of Government securities held by banks during the developing recession from October 1957 through June 1958.)

3. *Distribution of securities profits among banks.*—Bank profits on securities are divided between large and small banks in much the same ratio as other indicators of bank operations.

There are 49 banks in the country which have \$500 million or more in total deposits. These banks had securities profits of \$299 million in 1958, or 44 percent of the total profits on securities by all 13,000 insured commercial banks. The same 49 banks accounted for 39 percent of total bank assets and 42 percent of total current bank earnings. These same banks paid 49 percent of the taxes of all banks, had 38 percent of total bank deposits, and accounted for 40 percent of the total capital accounts of all banks. Thus large banks accounted for just about the same proportion of total bank securities profits last year as they showed on total assets, earnings, taxes, or capital.

I do want to say that as far as the 17 primary dealers are concerned, as I understand, the Federal Reserve bank is perfectly willing to do business with anybody in the country who wants to get in and become a dealer. There happen to be 17 primary dealers and a few others which are more specialized in one kind of Government issue. There is a problem here that we have inquired into that I think will come out in the factual data—as to why there are not more than that.

Senator JAVITS. That is all I have in mind, to give a balanced picture. I think that all this may be a sideshow in what you are being essentially questioned about here. Still, we ought to have a balanced picture.

As to the questioning which has just taken place by Congressman Reuss, let me ask you this: Is there any doctrinaire objection on the part of the Treasury which will inhibit the United States from becoming an open market purchaser of Government bonds?

Secretary ANDERSON. Senator Javits, it seems to me that the monetary authorities ought to have a maximum of flexibility as to how the detailed instruments of the monetary authorities are used from time to time. Certainly it is within the right and the power of Congress if you choose to give detailed instructions as to how they might be used. I myself would not think that the course of wisdom. Rather, I would think the course of wisdom to be one of setting out objectives, matters of national policy, goals that we try to achieve, and of relying upon the monetary authorities to use the various instrumentalities they have in order to be the most helpful to the whole economy of our country.

Senator JAVITS. Do I understand you to say, therefore, that there is no inhibition in the Treasury about open-market purchases?

Secretary ANDERSON. No; we have no inhibition.

Senator JAVITS. Let me get to the substance of your testimony, which I think is rather important here.

I notice at page 7 you say that a larger volume of production can only take place if you have more equipment, and that may very well have to be done "at the expense of current consumption."

Do you hold with the President that as we see the situation now, we cannot contemplate any tax reduction?

Secretary ANDERSON. I hold with the President exactly. What we have to do is to say that we have an obligation with respect to our national debt; that just the mere fact that there may be on the horizon a possibility, a reasonable hope, of having some more revenues than we have expenditures, does not lead us to conclude that we can ignore the debt and thereby reduce taxes.

I think, on the other hand, that the hearings which will take place in the fall with reference to tax changes ought to be considered in the light of the contribution that they could make both toward equity and toward benefits to the whole economy.

Senator JAVITS. Is there any other way, except in the tax level, that the Federal Government can help to bring about the siphoning off of more of the public's income to the building up of our productive resources?

Secretary ANDERSON. All of our resources, of course, that we spend come either through taxes, customs, or some other form of assessments.

Senator JAVITS. In other words, if the public would choose itself to save more money beyond the tax level. Is there anything else the Treasury can do about that?

Secretary ANDERSON. In an economy like ours, the public itself must decide how much goes for consumer goods, how much for savings, and how much for investment.

Senator JAVITS. A very distinguished economist who has been participating in this debate, Leon Keyserling, talks about a good deal of economic slack in the economy. Yet I notice that you say that we have been pretty much using all of our plant equipment and, I assume, personnel to the maximum. Would you care to make any comment about that? Incidentally, as you may know, I am not of the school that believes we are giving sufficient attention to trying to beat the Russians. I think this is a very important part of the whole picture, and we are not taking enough account of that.

But Keyserling says there is a lot of slack in the economy; we are not using our resources to the full. You seem to think we are. Would you comment on that?

Secretary ANDERSON. The comment I made here refers to a broad period. I think over that period we have generally used our resources rather fully.

There are periods, if you want to take, for example, periods last year, when we certainly had excess plant capacity and unemployment. I also point out in the statement the biggest single enemy to continuity of growth in our country is recession. How do you prevent recessions?

Recession is an adjustment to something. It is not something which anybody in our country wants. But if you bunch together the capital expenditures and then there is a very sharp decline, if you bunch together expansion and there is a sharp decline, if inflationary pressures are built up and we have to adjust to them, we go through these recessionary periods.

What we are trying to achieve and what I was trying to say is, How do we have, as nearly as we can, a sustained rate of high level of the use of our total resources?

This, it seems to me, requires that we utilize to the maximum the ingenuity, capacity, freedom, technological advances, and all of that in our country, and that we also encourage the savings out of which these various plant additions can be made, so that the million people that are coming into the market every year have a place that they can work, and that we avoid the readjustments which can follow too rapid an expansion, with inflationary pressures.

Senator JAVITS. Mr. Secretary, I have just two other questions, if I may ask them, with the chairman's indulgence. One is this:

Talking about savings, 15 percent of our debt is now held in the savings bonds. Do you believe that the United States would benefit if we had very materially increased the percentage of the debt which is held by savings, and that, therefore, that should lead us to some massive effort beyond the effort we are undertaking today, on that score?

Secretary ANDERSON. Senator Javits, the savings bonds which are held by those individuals are one of the best places, certainly, for the savings to be held. To be very frank, if through what we are asking now on E and H bonds we will just be able to keep our own on all kinds of savings bonds and hold our position for the next year or two, I will think we have done a pretty good job. I would like to see it expanded. But even with great effort, I would not be unhappy if we just held our position.

Senator JAVITS. And that goes for the savings bonds, too?

Secretary ANDERSON. I am including those savings bonds like the F's and G's and J's and K's, which we no longer issue, but which are currently outstanding, as well as our E's and H's.

Senator JAVITS. So that you feel that for the next 2 years your problem is one of not slipping back, rather than of going forward?

Secretary ANDERSON. Yes. We would increase the E and H in order to offset the cash-ins and the maturities of the F's, G's, J's, and K's.

That is not to say that any increase is not desirable. I am talking about the fact that if we are able to hold our own, we would feel

pretty good about it. If we are able to make some slight gain, we would feel better.

Senator JAVITS. I gather you would like to expand the savings bonds if you could?

Secretary ANDERSON. That is correct.

Senator JAVITS. I have just one last question.

In this present strong feeling in the administration about the budget, is there any differentiation as to what you spend your money for, or is all expenditure put in the same category? That is, is defense put in the same category with housing and farm price supports, or is there not some distinction about expenditures, which is as you say yourself, in what I consider to be an excellent statement:

Expenditures for goods the people did not want which ended up in warehouses being given away or destroyed, or expenditures for goods which people did want and use.

Is there any such differentiation in your Federal budget? And if so, how is it reflected?

Secretary ANDERSON. In the first place, monetarily, whatever we pay the money out for has the same kind of budgetary impact.

Philosophically, it seems what a nation like ours must do is to say to itself, you must first do everything that is necessary for your country to do. This would certainly include an adequate defense. Then, you do as much as seems desirable as you can afford to do at any given time. The fact that perhaps you cannot afford to do everything that is desirable at any given time does not lessen its desirability. It simply means that you do not try to do everything that is desirable plus everything that is necessary at the same time.

Senator JAVITS. But what about the proposition of what adds to the wealth of your country and what goes down the drain? Even defense does not add to the wealth of your country, but housing does. Why not make a differential therefore? Suppose you wrote into your budget \$2 billion for homes. That would add many times that total value to the country. Why not include that in your calculations on the budget and in terms of the credit of the United States?

Secretary ANDERSON. I think what you could do, if you simply add on these additional things, whatever they may be, you add them on at the cost of putting on inflationary pressures that drive the ultimate cost of the things up, and in the long run either bring about readjustments or make it impossible for people to buy the things they want because the price gets too high.

If this country just undertakes to continually run a deficit, we can only get this money out in two ways: We have either to tax for it or to borrow it. If we continue to borrow and never to pay, then we run these dangers of inflation.

Senator JAVITS. Thank you, Mr. Secretary. I think it is an excellent exposition of the point.

The CHAIRMAN. Representative Coffin?

Representative COFFIN. Thank you, Mr. Chairman.

Mr. Secretary, I wanted to ask a very simple question, prefacing it with these statements.

If you wanted desperately to get a better maturity curve on your long-term securities, you would like to sell your securities at the lowest possible rate of interest. We have had some colloquy about an un-

easiness prevailing because we do not know why, because there are so few dealers, we are getting the best possible break when we do sell to the market. You in your statement have said the market cannot fail to be improved by more active competition.

You auction your bills now, and sometimes you auction securities of a longer term than the bills. My question is, before we jump into the higher interest rate or remove the ceiling in order to make sure that this is necessary, why do we not have a try at auctioning some of our new long-term issues?

This is not the auction to which you addressed your remarks in your statement. I am not talking about an auction within the exchange for all the securities, new and old. I am just talking about making an experiment, trying to induce an auctioning of long-term issues to see what would happen. What are your views on this?

Secretary ANDERSON. With the Congressman's permission and the chairman's permission, I would like to respond perhaps briefly and then amplify my statement with a longer statement, because you have asked a very pertinent question.

I should like to say first that nothing would please me more than to believe and to hope that every security which the U.S. Treasury sold could be auctioned. It would certainly relieve us of a major responsibility in pricing and selling coupon issues where we have to fix the rate. Traditionally, of course, as you have said, we have auctioned the 91-day bill. In more recent months we have begun the auction of 6 months' bills. More recently still, we have begun the auction of yearly bills, working toward four quarterly dates for the yearly bills, when they will be auctioned.

When we get into the longer terms, we run into a number of problems. In the first place, the auction technique is not one that is known well to a multitude of people over the country. It requires a great deal of professional capacity in order to buy at auction a Government security, and particularly a long-term Government security, when a small amount of rate change could have a much larger effect on price than an equivalent change of rate would have on the price of a short-term security.

If one looks at what happens in other markets, for example, and goes back to the first of this year, almost every municipal issue that I know about that has been \$100 million or more has received only one bid. I think maybe there was only one exception.

These bids were made up by syndicates. There is a distinction, because they were bidding at that time on an all-or-none basis. Because they bought all or none, they had a greater flexibility in the way in which they get rid of their securities.

When the local housing authority mortgages were offered in something like \$100 million, which was guaranteed by the Federal Government, again there was only one bid.

If, therefore, we went into the market, not with \$100 million but with \$2.5 billion or some other large amount, we might, rather than increase the number of bidders, find that we would have only one or a few bids, or maybe not even enough of a combination between syndicates so that they would be willing to take it at all.

Representative COFFIN. Which you would not know until you tried it.

Secretary ANDERSON. I think one could gage pretty carefully the fact that if municipalities who sell their securities in \$100 million lots got one or two bids, we could not hope, if we set out for a billion dollars, to get a great number of them.

Representative COFFIN. Is this not a reaction in part because of the first reason you gave; namely, because of lack of certainty or assurance by dealers in going in for a long-term bid, or a rather large bid?

Secretary ANDERSON. The first reason I cited was that a good many people did not have the capacity, the professional capacity, in the country banks and that sort of thing, so they can buy what they want on a coupon, but they would be pretty hard pressed if they could buy only from the Treasury by submitting a bid.

Representative COFFIN. I would be very despondent if I felt that we could plunge into outer space and nuclear weaponry and all that, and yet feel that the mystic arrangements of the market could not be communicated to enough people to bring competition to this very vital area. I would think that perhaps you would be advised to explore ways and means of distributing information, of educating in this auction technique the people in the market now, and others who might enter it. Are we to remain resigned to the fact that this is a field that can only be known by a very few people who can move with assurance in it?

Secretary ANDERSON. No, Congressman; I would not want to indicate any reluctance whatsoever to explore, study, and get the best judgments from everybody in the country on how it might be done.

Representative COFFIN. Have you made any surveys or studies with regard to the practicability of engaging in auction techniques for the longer term issues of new securities?

Secretary ANDERSON. We continually talk to people of all classes of investors as to whether or not an enlargement of auctioning might be feasible.

Representative COFFIN. I am not really interested in your continual discussions. I know you must do that on virtually every phase of your operations. But I am talking about a focused study such as you made with regard to the auction within the exchange, a deliberate attempt to explore this with the possibility that this might give you a tool which you could use in your very difficult task of marketing.

Secretary ANDERSON. I would say that there have been various times of highly concentrated study in this area. We have not singled out just one project and said that this is the only point of reference. The paper I'm submitting for the record goes into the whole matter quite carefully.

There is one other thing I would like to suggest here, and that is that under our tax statutes, if one pursues an auction of all securities, he gets into some very highly complex problems in which the rate of tax that would be paid by various holders is dependent not only upon the price at which they buy the security—and there would be many different issue prices in an auction—but is dependent in part upon whether, during the life of the security, say a 10-year bond, they sell at a higher or lower price.

At present you would have to have almost a genealogy of some of these securities in order to know the price which determines how taxes were going to be paid.

This is a problem upon which we have given a considerable amount of study. Rather than try to expound it here, because it is highly technical, I will furnish it to the committee in the statement.

Representative COFFIN. The committee, I am sure, would appreciate getting as deliberate a statement on this as possible, and also whether or not you contemplate looking into this problem to a great extent.

I think it might be a more practicable alternative than the type of auction to which you addressed your remarks in your joint statement.

(The statement referred to is as follows:)

SELLING TREASURY SECURITIES THROUGH AUCTION

1. *Use of auction for short-term securities.*—Since 1929 the Treasury has sold short-term Treasury bills—mostly with a 91-day maturity—through competitive bidding in an auction rather than by Treasury fixing a price and interest return to the investor directly. This has been an efficient mechanism for establishing a more or less routine payoff and new issuance of as much as \$1.8 billion of new bills each week. These auctions are conducted through sealed bids submitted in writing within a specified time limit to any Federal Reserve bank or branch. (Typical Treasury announcements of a bill offering and the results are attached).

The auction technique has been extended beyond the routine 91-day bill operation. Beginning in 1951 the Treasury sold tax anticipation bills through auction, and since then as much as \$8 billion a year of tax anticipation bills have been marketed in this way. A further extension of the auction technique was introduced last December when the Treasury announced its new cycle of 6-month bills in addition to the regular 3-month bills.

In March 1959, the Treasury took another important step in the use of the auction technique by announcing the first of a series of four issues of 1-year Treasury bills to mature at quarterly intervals. The hope was expressed at that time that the greater use of the auction technique for a security as long as 1 year would permit some reduction in the amount of 1-year certificates which the Treasury has to price. As of July 15, 1959, therefore, the Treasury has \$37 billion of Treasury bills outstanding, all of which were sold at auction, as compared with \$22½ billion a year ago, and \$13½ billion right after the Treasury-Federal Reserve accord 8 years ago.

The Treasury has obviously concluded, therefore, that there is considerable merit in the extensive use of the auction technique in selling short-term securities. These issues, however, are bought almost entirely in large amounts by professional investors who are thoroughly familiar with the money market on a day-to-day basis.

2. *Could the auction technique be extended to long-term bonds?*—A major objective of Treasury debt management policy is, of course, to get as broad a distribution of public debt as possible. In this way more of the debt can be placed in the hands of longer term investors. Real savings can be tapped and less reliance is needed on borrowing from commercial banks. The Treasury has from time to time given careful consideration to the possibility of extending the competitive bidding system used on Treasury bills to longer term securities. We do not believe, however, that in the present market environment such a step would be in the public interest.

Subscriptions to new offerings of Treasury certificates, notes, and bonds issued on a fixed price basis are made by thousands of small banks, corporations, associations, and individuals throughout the country. Most of these investors do not have enough current background data to submit a carefully prepared bid for these securities. If the competitive procedure were used, therefore, the Treasury could be in a position of impairing the opportunity now open to small- and medium-sized investors of buying new securities directly from the Treasury. This might be taken to imply that we aren't interested in their having a chance to buy from the Treasury on the same terms as large investors.

Furthermore, on fixed price issues the Treasury can more easily control the amount issued to any single investor or investor class than it could on an auction. Total subscriptions from commercial banks on medium and longer term

bonds, for example, are typically limited to a certain percentage of capital and surplus and on occasion subscription limitations from other types of investors have been used. Substantial downpayments are also often required to minimize speculation. Allotments in full are always made to small investors. In addition allotments (actual security issuances) to different investor groups may vary considerably, with preference usually given to savings-type investors. The allotment procedure, in particular, would be extremely difficult to use in connection with an auction, and there would be difficulty in adapting other successful marketing techniques to the auction method.

Another way of looking at it is that the competitive situations arising from the auction technique in handling short Treasury issues versus long Treasury issues are quite different. In the auction of a short-term security the professional underwriters who purchase for secondary distribution are competing not only among themselves but are also competing with a large number of professional buyers who are purchasing for their own investment needs. Thus, the market underwriters have to consider not only the underwriting competition but they also have to submit bids that are competitive with those submitted by the primary investors who are well acquainted with this market technique.

On the other hand, in a longer term issue the use of the auction instrument would undoubtedly generate bids almost exclusively from the professional underwriters, both dealers and banks, who would then do the secondary distribution. In this case the professional underwriters have to worry only about their underwriting competition and do not have the competitive influence of informed bids submitted by primary investors.

It should also be mentioned that most new Treasury securities are not issued for cash at all but are offered in exchange for maturing securities. Use of the competitive bidding system on all new securities would mean, presumably, that the Treasury would pay off all maturing issues in cash and issue new securities. At the present time, most holders of maturing issues—again, many of them small holders—simply turn in the old security for the new one. If, however, each holder has to enter a competitive bid for the new securities, he again runs the risk of being left out and of having to buy the securities back from some successful bidder.

Competitive bidding for all new issues would also tend to add to the amount of purchases by those buyers familiar with bidding techniques who would submit bids at relatively low prices just on the chance that they would be accepted. This would be particularly true in a period where interest rates are rising and credit is not so readily available. In such periods, reluctant buyers would tend to indicate their lack of enthusiasm for Government securities by offering low bids (high-interest rates). One result of competitive bidding under such circumstances would therefore tend to be a net increase in the cost of interest on the public debt to the Treasury—and to the taxpayer.

In addition, if the successful bids were so low as to produce interest rates on the new securities well above the market, the entire market could be upset, with unfortunate implications for both debt management and monetary policy. In many instances, therefore, too great use of competitive bidding would tend to prevent the Treasury from fully exercising its debt management responsibilities.

On long-term issues the problem of the leverage effect of a small-yield difference in causing a large difference in price comes into play. An eighth of 1 percent spread in yield on a 91-day bill is worth only 31 cents on a \$1,000 bond. On a 1-year issue it is worth \$1.25 per \$1,000, and on a 40-year bond it is worth \$50. That means that even though the high and low accepted bids on a 40-year bond are within a seemingly narrow range of one-eighth of 1 percent the price range would be all the way from \$950 to \$1,000. Let us assume that the average bid accepted is \$975. As a result, the bidder who happened to get his bid accepted at \$950, the "tail bidder," is encouraged to sell his bond immediately for a quick speculative profit as long as the market price is well above his cost. If many of those who bought bonds cheaper than the average do this, of course, their profits will shrink as the price goes down, but in the process they will have succeeded in knocking the market down and interfered with the orderly distribution of the issues by legitimate underwriters to ultimate owners. The secondary distribution of an auctioned bond would be further impaired, of course, by the obvious reluctance of successful bidders who paid above the average price to take a loss on the transaction at the market price even if it remains steady at the average bid.

Two more points may be made. Many institutional portfolio managers dislike the auction technique because they have to pick a price. If they bid high enough to insure buying the new securities they probably will be above the average accepted bid and will be subject to the criticism of their own institution that they paid too much. If they try to be sure to get under the average they may be outside the range of accepted bids, and come away from the auction (which is, of course, based on sealed bids) with nothing. Since there is always the secondary market to fall back on, many investors prefer to take the latter chance rather than the former, thus tending to lower the average price and increase the cost to the Treasury.

The other point also relates to investor attitudes. Quite apart from tax considerations, the basic preference by investors in Governments is for issuance at par. Many investors "buy coupon"; that is, they want as high a rate of current earnings as they can get rather than the same overall income consisting of lower current earnings plus a capital gain when they sell the bond or it matures. These investors (such as pension funds) prefer to buy a $4\frac{1}{4}$ percent 10-year bond at par yielding $4\frac{1}{4}$ percent to a $3\frac{3}{4}$ percent 10-year bond at a little under 92, also yielding $4\frac{1}{4}$ percent. On the other hand, many investors prefer not to buy at a premium because they don't like to get part of their capital back with each interest payment.

During the 1930's the Treasury used the auction method of selling some long-term bonds, both with reference to its own issues and to Federal agency issues. Market performance in the distribution of the bonds was reported to be unsatisfactory, as indicated in a staff memorandum which is included at the end of this statement.

3. *Competitive bidding for other securities.*—It has also been suggested that perhaps the Treasury could sell its longer securities by competitive bids in the same manner used by corporations and State and local governments in their sales of longer term issues rather than doing it by the same method used in auctioning bills. In State and local and corporate issues rival underwriting syndicates each typically submit bids to take all or none of the securities offered, with bids that include an allowance, of course, for profit to the underwriter. The bidders prefer the "all or none" approach. If they only bid for part of an issue there probably would be practically no bids at all since no dealer would take a substantial position if he was taking the chance that he might be at the mercy of other dealers who bid less.

Any attempt to apply the syndicate idea to Government securities would present many problems, however. U.S. Government issues dwarf in size the issues of any other borrower. During the calendar year 1958, for example, the Treasury sold $\$48\frac{1}{2}$ billion of new securities to the public. Only 13 issues of bonds, notes, and certificates were involved (other than the additions of \$100 to \$200 million a week in bill rollovers) or an average size of issue of about $\$3\frac{3}{4}$ billion. By contrast, the largest single corporation issue floated in 1958 was only \$350 million, and the largest single State and local government issue somewhat less. No syndicate large enough to handle market issues of Government securities could be formed without its being so large as to dominate the entire market, both with respect to the Treasury and to ultimate investors. This would not be good public policy.

It should also be mentioned that so far this year all but one of the State or local government issues offered in "competitive" bidding in amounts of \$100 million or more attracted only one underwriting bid, on an "all or none basis." (See attached table.) This suggests that the very size of new municipal debt issues severely strains the capacity of bond underwriters. The resources of securities underwriters would obviously be completely inadequate to handle competitive bidding on Treasury bonds.

4. *Tax complications of auctioning.*—In an auction of any coupon issue it would still be necessary for the Treasury to price issues to some extent since a coupon rate has to be placed on the security in any event. However, no bid could be accepted below a certain discount under par without tax complications. If the discount were less than one-fourth of 1 percent below par for each full year to maturity on the new security, the increase in value to par would be a capital gain. But securities issued at any greater discount would be subject to the tax law provisions governing original issue discount, and the increase in value to par in this case would be taxed as ordinary income, with a proration based on time if more than one holder is involved. These provisions do not apply to bills since they are not a capital asset and all increases in value are taxed as ordinary income.

This would not be as great a problem if the Treasury issued all such securities at the same price. But with an auction, bids may be accepted at a great many different prices. Each of these securities issued in acceptance of varying bids would have a different original issue discount under the tax law. Furthermore, even securities issued with the original issue discount might be accorded different tax treatment as the result of transactions in the secondary market. In addition to producing a multiplicity of slightly differing types of the same issue in the market, this would create additional confusion in evaluating them. Thus, investor interest in such issues would be effectively undermined.

5. *Conclusion.*—The Treasury believes, therefore, that there are formidable obstacles in the path of any successful application of the auction technique to intermediate or longer term bonds. We are pleased, however, with the results to date of the rapid expansion of the auction technique in the very short term area which we have undertaken recently, and certainly do not foreclose the possibility of further expansion of auctions in that area. We believe further that the present practice of offering Treasury certificates, notes, and bonds at prices and interest rates determined by the Treasury does result in an effective distribution of new Treasury issues at minimum cost to the taxpayer. In the last analysis, a potential buyer of a new Treasury issue must find the rate of interest attractive or he will prefer to buy a security in the outstanding market regardless of whether the Treasury evaluates that attractiveness for him by setting a price, or whether he tries to measure the amount of attractiveness himself in terms of submitting a bid.

[Release Thursday, July 16, 1959]

TREASURY DEPARTMENT,
Washington, D.C.

A-574.

The Treasury Department, by this public notice, invites tenders for two series of Treasury bills to the aggregate amount of \$1,400 million, or thereabouts, for cash and in exchange for Treasury bills maturing July 23, 1959, in the amount of \$1,400,956,000, as follows:

Bills (91-day) (to maturity date) to be issued July 23, 1959, in the amount of \$1 billion, or thereabouts, representing an additional amount of bills dated April 23, 1959, and to mature October 22, 1959, originally issued in the amount of \$400,070,000, the additional and original bills to be freely interchangeable.

Bills (182-day) for \$400 million, or thereabouts, to be dated July 23, 1959, and to mature January 21, 1960.

The bills of both series will be issued on a discount basis under competitive and noncompetitive bidding as hereinafter provided, and at maturity their face amount will be payable without interest. They will be issued in bearer form only, and in denominations of \$1,000, \$5,000, \$10,000, \$100,000, \$500,000, and \$1 million (maturity value).

Tenders will be received at Federal Reserve banks and branches up to the closing hour; 1:30 p.m., eastern daylight time, Monday, July 20, 1959. Tenders will not be received at the Treasury Department, Washington. Each tender must be for an even multiple of \$1,000, and in the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals; e.g., 99.925. Fractions may not be used. It is urged that tenders be made on the printed forms and forwarded in the special envelopes which will be supplied by Federal Reserve banks or branches on application therefor.

Others than banking institutions will not be permitted to submit tenders except for their own account. Tenders will be received without deposit from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. Tenders from others must be accompanied by payment of 2 percent of the face amount of Treasury bills applied for, unless the tenders are accompanied by an express guarantee of payment by an incorporated bank or trust company.

Immediately after the closing hour, tenders will be opened at the Federal Reserve banks and branches, following which public announcement will be made by the Treasury Department of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection thereof. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and his action in any such respect shall be final. Subject to these reservations, noncompetitive tenders for \$200,000 or less for

the additional bills dated April 23, 1959 (91 days remaining until maturity date on October 22, 1959), and noncompetitive tenders for \$100,000 or less for the 182-day bills, without stated price from any one bidder, will be accepted in full at the average price (in three decimals) of accepted competitive bids for the respective issues. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve bank on July 23, 1959, in cash or other immediately available funds or in a like face amount of Treasury bills maturing July 23, 1959. Cash and exchange tenders will receive equal treatment. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

The income derived from Treasury bills, whether interest or gain from the sale or other disposition of the bills, does not have any exemption, as such, and loss from the sale or other disposition of Treasury bills does not have any special treatment, as such, under the Internal Revenue Code of 1954. The bills are subject to estate, inheritance, gift, or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority. For purposes of taxation the amount of discount at which Treasury bills are originally sold by the United States is considered to be interest. Under sections 454(b) and 1221(5) of the Internal Revenue Code of 1954 the amount of discount at which bills issued hereunder are sold is not considered to accrue until such bills are sold, redeemed, or otherwise disposed of, and such bills are excluded from consideration as capital assets. Accordingly, the owner of Treasury bills (other than life insurance companies) issued hereunder need include in his income tax return only the difference between the price paid for such bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made, as ordinary gain or loss.

Treasury Department Circular No. 418, revised, and this notice, prescribe the terms of the Treasury bills and govern the conditions of their issue. Copies of the circular may be obtained from any Federal Reserve bank or branch.

[Release Tuesday, July 21, 1959]

TREASURY DEPARTMENT,
Washington, D.C.

A-583.

The Treasury Department announced last evening that the tenders for two series of Treasury bills, one series to be an additional issue of the bills dated April 23, 1959, and the other series to be dated July 23, 1959, which were offered on July 16, were opened at the Federal Reserve banks on July 20. Tenders were invited for \$1 billion; or thereabouts, of 91-day bills and for \$400 million, or thereabouts, of 182-day bills. The details of the two series are as follows:

Range of accepted competitive bids	91-day Treasury bills maturing Oct. 22, 1959		182-day Treasury bills maturing Jan. 21, 1960	
	Price	Approximate equivalent annual rate	Price	Approximate equivalent annual rate
		<i>Percent</i>		<i>Percent</i>
High.....	\$99.171	3.280	\$98.061	3.835
Low.....	99.154	3.347	98.032	3.893
Average.....	99.156	3.337	98.044	3.869

NOTE.—84 percent of the amount of 91-day bills bid for at the low price was accepted; 20 percent of the amount of 182-day bills bid for at the low price was accepted.

Total tenders applied for and accepted by Federal Reserve districts

District	Applied for	Accepted	Applied for	Accepted
Boston.....	\$34,942,000	\$24,905,000	\$3,467,000	\$3,367,000
New York.....	1,442,556,000	647,019,000	565,275,000	245,254,000
Philadelphia.....	29,087,000	13,062,000	12,642,000	7,642,000
Cleveland.....	32,823,000	32,393,000	10,935,000	10,535,000
Richmond.....	15,522,000	13,722,000	5,868,000	5,868,000
Atlanta.....	41,138,000	18,320,000	3,919,000	3,069,000
Chicago.....	201,611,000	120,711,000	73,581,000	63,531,000
St. Louis.....	18,352,000	15,866,000	4,420,000	4,420,000
Minneapolis.....	6,990,000	6,990,000	8,731,000	7,971,000
Kansas City.....	37,986,000	33,728,000	7,306,000	6,906,000
Dallas.....	20,444,000	20,021,000	3,322,000	3,322,000
San Francisco.....	63,685,000	53,343,000	38,652,000	38,252,000
Total.....	1,945,136,000	1,000,080,000 ¹	738,118,000 ²	400,137,000

¹ Includes \$241,660,000 noncompetitive tenders accepted at the average price of \$99.156.

² Includes \$48,648,000 noncompetitive tenders accepted at the average price of \$98.044.

Bids for large municipal bond offerings (generally \$25 million and over)

Date of bid	Amount		Type	Number of bids	Range of bids
<i>1939</i>	<i>Millions</i>				
July 15	\$31	Ohio, highway.....	S.T.	2	3.54 to 3.57 percent.
June 30	195	Grant County Public Utility District.....	Rev.	1	(300 member A/C).
30	25	Maryland.....	Rev.	2	4.02 and 4.05 percent.
30	50	New York State.....	G.O.	2	3.35 and 3.36 percent.
17	30	Port of New York Authority.....	.....	2	4.09 and 4.11 percent.
10	63	Connecticut.....	Rev.	1	4.30 percent.
10	100	California.....	G.O.	1	3.95 percent merged syndicate.
4	27	New York City.....	G.O.	2	
2	40	Los Angeles F.C.....	.....	1	2 syndicates merged.
May 27	30	Chicago, Ill.....	Rev.	5	4.05, 4.18, 4.19, 4.25, and 4.26 percent.
26	105	New Housing Authority.....	P.H.A.	1	3.78 percent. Bankers and dealers groups merged.
13	25	New Jersey.....	G.O.	4	3.24, 3.26, 3.27, 3.28 percent.
12	27	Cincinnati, Ohio.....	G.O.	2	3.47, 3.48 percent.
Apr. 22	33	Oregon.....	G.O.	3	3.39, 3.43, 3.53 percent.
21	200	New York State Power Authority.....	Rev.	1	4.21 percent.
14	60	Massachusetts.....	G.O.	1	3.46 percent, 3 syndicates merged "due to thinness of the market."
9	25	Florida Development Commission.....	Rev.	3	4.10, 4.13, 4.14 percent.
9	53	Massachusetts Turnpike Authority.....	Rev.	1	
7	27	Los Angeles School District.....	G.O.	2	3.44 and (not available).
Mar. 31	30	Pennsylvania General State Authority.....	.....	2	3.58, 3.65 percent.
17	29	Baltimore, Md.....	G.O.	2	3.11, 3.14 percent.
11	100	California.....	G.O.	1	3.55 percent merged account.
10	26	Southern California Metropolitan Water District.....	G.O.	2	2.96, 3.10 percent.
10	26	New York City.....	G.O.	2	3.17, 3.21 percent.
5	30	Port of New York Authority.....	G.O.	2	3.68, 3.69 percent.
4	25	Philadelphia, Pa.....	G.O.	3	3.27, 3.31, 3.33 percent.
3	25	Michigan, Expressway.....	S.T.	2	3.54, 3.63 percent.
Feb. 26	104	New Housing Authority.....	P.H.A.	2	3.41 percent (\$69 million to bank group—\$35 million to dealer group).
25	40	Chicago, Ill.....	G.O.	2	3.20 and 3.26 percent.
18	25	East Bay Municipal District of California.....	G.O.	3	3.45, 3.46, 3.51 percent.
Feb. 18	60	New York State.....	G.O.	2	2.91, 2.93 percent (winning bid—a merged a/c).
16	120	Chicago, O'Hare Airport.....	Rev.	1	
10	25	Washington (State).....	G.O.	3	3.17, 3.19, 3.20 percent.
10	23	Minnesota (State).....	G.O.	1	
4	20	Los Angeles.....	G.O.	4	3.47, 3.48, 3.50, 3.52 percent.
3	72	Massachusetts Port Authority.....	Rev.	1	
Jan. 28	20	Puerto Rico.....	G.O.	2	3.94, 3.97 percent.
27	20	Houston, Tex.....	G.O.	3	3.48, 3.51, 3.52 percent.
28	20	New York City Housing Authority.....	.....	3	4.07, 4.17, 4.18 percent.
21	20	Oregon.....	G.O.	3	2.77, 2.82, 2.83 percent.
15	25	Sacramento Municipal Utilities District.....	Rev.	2	3.58, 3.62 percent.
6	200	New York State Power Authority.....	Rev.	1	

¹ Negotiated with underwriters.

G.O. General obligations.

S.T. Special tax fund.

Rev. Revenue.

SELLING U.S. GOVERNMENT DIRECT AND GUARANTEED ISSUES BY TENDER

[Excerpts from staff memorandum prepared in September 1940]

With respect to the broad use of the tender method in the sale of securities by the Treasury, the proponents of this method, prior to the actual operation of the plan in selling direct and guaranteed securities in 1934 and 1935, believed that there were several distinct advantages compared with the regular quarterly offerings by subscription. These were as follows:

1. The Treasury could obtain required funds at a minimum interest cost.
2. Market conditions would tend to be more stable, since the Treasury could do its financing when the market was strong, and could remain out of the market during periods of weakness.
3. The Treasury would not be forced to accept prevailing market conditions on the quarterly dates.
4. The method would permit small issues to be increased gradually from time to time by subsequent offerings, in whatever amounts the Treasury saw fit to issue.

Contrary to these expectations, however, the market voiced disapproval of the tender method after it had been in use for a while. Although the poor reception given to the last few offerings on tenders was undoubtedly influenced somewhat by other factors unsettling to the market, several important criticisms of the tender method were made as follows:

1. Initial distribution was sharply restricted. Many banks and investors outside of the largest centers felt that they were not in a position to gage the market with any degree of accuracy, and those who did submit bids generally paid the highest prices. The largest portion of the new issues awarded above the average price for each went to bidders outside New York City, while most of the amounts awarded at or below the average went to banks, brokers, and dealers in New York. New York City banks and dealers bid for about two-thirds of the accepted total; and of the two most successful issues, 82 and 83 percent, respectively, were taken in the New York district.

2. After the first issues, the market became somewhat nervous over the extent to which the tender method was to be employed. Due to uncertainty as to the time, size, and frequency of such offerings, they had the same effect on the market as if a known seller was waiting to dispose of a very substantial block of bonds at any time. Banks and dealers were unwilling to make commitments as freely, and the market generally was not afforded sufficient respite in which to absorb the offerings. This was especially important because the initial distribution was not as comprehensive as usual.

3. The profit inducement was practically wiped out, in that the almost certain market premium on issues offered in the regular way, which had served as an inducement to smaller banks and others to subscribe, was eliminated. The market believed that under the competitive bidding method the probable profit would be small and uncertain, and many investors, feeling that the prospective small profit did not justify the risk involved, refrained from bidding. This was particularly true after the out-of-town institutions bid for the new bonds near the current market, only to find the dealers and larger banks receiving sizable amounts at prices substantially under the market.

Even this latter group seemed dissatisfied with the profit available, although there apparently was short selling in the market against bids for the new issues placed below current levels. Generally, the underwriting margins were smaller and more precarious, while secondary distribution was made difficult by the frequency of offerings.

4. There appeared to be an increasing tendency toward lower prices. Prospects of a continued supply resulted in the dropping of bids by dealers and the larger investors in close contact with the market. This, coupled with short selling and the psychological effect of the increasing Federal debt were all factors pointing toward a decline in quotations. The short selling provided a cushion of bids by tender and under normal conditions might have been helpful but it is likely that the repeated selling against each offering had an undue influence on market prices.

In considering the merits of the tender method for selling large amounts at frequent intervals, of other than very short maturities, such as 90-day Treasury bills, there are several questions which seem to be worthy of consideration. Principally, they are:

1. Does the Treasury's aim of wide distribution into strong holders become realized?
2. Is general interest in Government securities stimulated and encouraged as much as it is by a definite offering at a price, which almost always has been heavily oversubscribed?
3. Can the Treasury be sure that any particular issue will be successful? Under the regular method, the Treasury has been able to insure the success of an issue by adjustment of the coupon rate and maturity date, but, in

offerings by tender there is no assurance that a satisfactory total of tenders will be received or that the bids will be within an acceptable price range.

4. Would the market reaction to a single large issue be as unfavorable as it was to frequent offerings of smaller amounts in an indefinite aggregate?

5. How does the cost of interest compare with that under the regular method?

6. Is there a political disadvantage in selling an additional series of an outstanding issue under the existing market price?

In order that a more detailed study of the tender method might be made, the remaining part of this memorandum is devoted to a brief review of the Treasury offerings by tender in 1934 and 1935, and to the details of each offering, including data concerning market conditions.

REVIEW OF OFFERINGS BY TENDER

With the exception of the regular Treasury bill issues and the \$50 million Panama Canal 3s (which were sold in March 1911 at an average price of around 102½) all of the direct and guaranteed issues sold on a tender basis were offered in 1934 and 1935. In July 1934, \$100 million Federal Farm Mortgage Corporation 3 percent bonds of 1944-49 were offered. (There were \$171 million of this issue outstanding at the end of June.) The action of the Treasury in handling the financing for a Government agency represented an innovation, and as the Treasury lacked discretion in fixing the coupon rate, it was decided to sell the issue by the tender method. In August, following weakness in the market due to European news, three new issues of short-term Home Owners Loan Corporation bonds, totaling \$150 million, were sold in the same manner.

No further financing of this nature was done until May 1935, when plans were formulated to apply the tender method to the offering of additional amounts of Treasury bonds. Press reports at the time stated that the Treasury believed this method would prove less disturbing to the market than the customary policy, and that the Government would obtain required funds at a minimum of cost. Accordingly, an offering was made on May 27, 1935, of \$100 million 3 percent Treasury bonds of 1946-48, of which there were \$825 million already outstanding. An additional lot of \$100 million of the 1946-48 issue was sold late in June, and three blocks of \$100 million each of 2½s of 1955-60, which were already outstanding in the amount of \$2,304 million, were offered on July 15, July 29, and August 12 respectively. The method became increasingly unpopular during this period, as indicated by the criticism which developed in the market and also by the fact that both the total tenders and the number of tenders received for the last two offerings were sharply lower than for the two immediately preceding. Notwithstanding the adverse comment, unsettled market conditions which had made some Treasury support necessary, and dwindling interest in the offerings, the Treasury offered \$100 million 1½ percent Federal Farm Mortgage Corporation bonds of 1939 on August 26. Total tenders amounted to only \$85,592,000, against which \$85,172,000 bonds were issued at an average price of 99. The offering was conceded to be a failure and the method was discontinued.

MARKET CONDITIONS MAY 15 TO SEPTEMBER 1, 1935

Prices of Treasury bonds were fairly steady, prior to the initial offering of 1946-48s on May 27, but a slightly easier tendency was apparent. The novelty of the tender system depressed prices temporarily, but these losses were regained in the next 2 weeks, and prices moved slowly upward until July 19 and 20. The market was quiet and fairly steady until August 1, but turned downward in August and losses ranging up to 2¼ points, took place between the early part of the month and August 27. There was an irregular upward reaction of as much as three-eighths of a point between August 27 and September 1.

Various external factors influenced the market during the latter part of this period, and undoubtedly increased its vulnerability to the disadvantages of the tender method. The main influence was the Ethiopian crisis, not yet at its peak, but already a disturbing factor. Some thought was also being given to inflation particularly in regard to certain aspects of the omnibus banking bill then before Congress, and to the administration pressure on Congress to dispose of several other measures by passing them as quickly as possible in order to speed up adjournment.

DETAILS OF INDIVIDUAL OFFERINGS

1. July 23, 1934—\$100 million 3-percent Federal Farm Mortgage Corporation bonds of 1944-49

These bonds were an additional series of the issue originally dated May 15, 1934, and of which there was a total of \$171,036,400 outstanding on June 30, 1934. On that date the total guaranteed debt amounted to \$680,767,817, including \$234,814,667 Reconstruction Finance Corporation notes, \$134,318,950 Home Owners Loan Corporation bonds, and \$140,597,800 other Federal Farm Mortgage Corporation bonds.

Immediately preceding the offering, the market had been quiet with a somewhat irregular tendency. Guaranteed obligations were firm, but turned easier after the announcement. The books closed on July 25, having remained open 3 days to permit full opportunity to subscribe, and by this time the issue had declined about one-half point. Other guaranteed issues were three thirty-seconds to eight thirty-seconds lower. Total bids of \$195,081,600 were received, and a total of \$100,260,300 was accepted at an average price of 100.559.

Price range

Accepted tenders:		
High	-----	102.250
Low	-----	100.438
Average	-----	100.559
Market price:		
Close July 22	-----	101 $\frac{1}{2}$ ³²
Low while books were open	-----	100 $\frac{21}{32}$

¹ 2.92 percent to call date.

On July 26, all markets turned downward after the assassination of Chancellor Dollfuss, and the Federal Farm Mortgage Corporation 3s closed at 99 $\frac{3}{32}$ bid. There was a rally of about one-fourth of a point on the following day, but prices of all U.S. issues declined sharply, and during the next 2 weeks the Federal Farm Mortgage Corporation 3s fell to 98 $\frac{30}{32}$ bid (on August 11).

2. August 6, 1934—\$50 million each of 1 $\frac{1}{2}$ -, 1 $\frac{3}{4}$ -, and 2-percent Home Owners Loan Corporation bonds of 1936, 1937 and 1938

These were new issues of short-term bonds, and the only other guaranteed Home Owners Loan Corporation issue outstanding was the 3-percent bond of 1944-52, of which there was \$283,546,000 outstanding at the end of July. Prices of both direct and guaranteed issues had been weak, following the assassination of Chancellor Dollfuss on July 25, and on July 26 there had been a drop of nearly a point, with a slightly lower tendency in evidence during the following week. After the announcement of this offering, quotations of guaranteed issues declined one thirty-second to five thirty-seconds further.

Total bids of \$233,126,600 were received for the three series combined, but only \$127,111,100 were accepted, the Treasury announcing that lower bids were not in line with market conditions. The prices of the issued bonds were as follows:

	High	Low	Average	Average yield
1 $\frac{1}{2}$ s	101.509	100.411	100.677	1.15
1 $\frac{3}{4}$ s	101.130	99	99.931	1.77
2s	101.035	99	99.962	2.01

Yields on Treasury notes of roughly comparable maturity were as follows (closing bid prices August 8, 1934):

	Percent
2 years (Aug. 1, 1936)	0.75
3 years 1 $\frac{1}{2}$ months (Sept. 15, 1937)	1.59
3 years 10 $\frac{1}{2}$ months (June 15, 1938)	1.77

Prices moved upward sharply (as much as 1 $\frac{1}{2}$ points for Treasury bonds) from August 11 to August 17, and the new Home Owners Loan Corporation issues gained about five-eighths of a point during this period. However, there

was renewed weakness as selling increased from August 17 to August 30, but the Home Owners Loan Corporation issues stood up well in the market, declining only about one-fourth of a point net compared with one-half of a point to one point for Treasury notes and bonds.

3. May 27, 1935—\$100 million (additional) 3-percent Treasury bonds of 1946-48

The Treasury announced an offering by tender of the 3s of 1946-48, of which \$82,507,900 had been sold in June 1934. An excerpt from the New York Times of May 27, 1935, indicates the Treasury's position regarding the tender method: "Treasury officials are understood to believe that the sale of bonds to the highest bidders will prove less disturbing to the money market than the former policy, and also that the Government will obtain the money it needs at a minimum cost. Under the policy of selling the bonds at stated figure it has been necessary for the Treasury so to gage the market's appetite as to assure the success of an offering, with the result that the interest rate has been slightly above the market.

Another explanation is that the Treasury is seeking to avoid the marketing of further issues carrying different interest rates than bonds already outstanding. The moment is considered opportune for the test of an offering of the type announced, as Government bonds have been enjoying a rising market."

The market had shown an easier tendency just prior to the announcement, and considerable price weakness resulted from it, although offerings were not large. The outstanding 1946-48s declined from $103^{27/32}$ to $103^{10/32}$ during the 3 days that the books were open. The rest of the market also moved lower, although short-term bonds showed only minor losses. Total bids of \$270,027,000 were received, and while a larger oversubscription had been expected, the operation was officially considered successful. Accepted bids ranged from $103^{26/32}$ to $103^{1/32}$.

4. June 24, 1935—\$100 million (additional) 3-percent Treasury bonds of 1946-48

Between May 29 and June 22 a moderate but steady improvement in prices occurred. The 1946-48s gained fourteen thirty-seconds. Other long-term bonds improved six thirty-seconds to nineteen thirty-seconds, while short-term bonds advanced about three-fourths of a point. On June 24 an additional \$100 million of the 3-percent Treasury bonds of 1946-48 were offered. The closing price prior to the announcement was $103^{20/32}$, the bonds remaining practically unchanged at this price throughout the 3-day period that the books were open. Tenders received for this offering were much larger in volume and at prices closer to the market than the previous offering. The shock of novelty appeared to have worn off and other influences on the market were more favorable. At the time of the first offering many dealers were said to have gone technically short of the 1946-48s, later purchases of the bonds causing a rally in price, but in this instance it was believed that few dealers were short. Bids totaling \$461,341,000 were received, of which \$112,669,000 were accepted at prices ranging from $103^{17/32}$ to $103^{24/32}$, or an average of $103^{18/32}$.

5. July 15, 1935—\$100 million (additional) 2 $\frac{7}{8}$ -percent Treasury bonds of 1955-60

Between June 26 and July 15 the long market was firm and somewhat higher. During this period, on July 8, there was a cash issue at par and accrued interest of \$500 million 1 $\frac{3}{8}$ -percent Treasury note of series B-1939 (due December 15, 1939). The coupon rate was looked upon as a new low for this type of financing. Subscriptions aggregating \$2,970 million were received and dealers reported a consistently strong demand for the new notes on a when-issued basis at prices ranging from 100 $16/32$ to 100 $20/32$.

The announcement July 11 of a probable additional offering on a tender basis of 2 $\frac{7}{8}$ -percent Treasury bonds of 1955-60 (the longest bond in the market, of which \$2,304,102,800 were already outstanding as of June 30) was well received by the market, although the price of this and several other long term issues declined several thirty-seconds. From July 15 to July 17, while the books were open, the price for the 1955-60s remained practically unchanged at 101 $20/32$, although the rest of the market advanced from $1/32$ to $5/32$. This offering was considered successful, total tenders for the country amounting to \$510,958,000. The tenders varied in price from 101 $27/32$ to 101 $19/32$, the average being 101 $19/32$.

6. *July 29, 1935—\$100 million (additional) 2½-percent Treasury bonds of 1955-60*

Prices of all direct Treasury issues were little changed between July 17 and July 29 when the sale by tender of an additional \$100 million 2½-percent bonds of 1955-60 was undertaken. This offering, although received less enthusiastically than was the similar offering 2 weeks earlier, influenced prices only slightly. While the books were open the market remained steady with nominal changes only, the 1955-60s selling at 101 20/32 high, 101 19/32 low and closing on July 31 at the latter price. Tenders aggregating \$320,981,000 were received, as compared with \$510,958,000 at the previous offering. The price range from 100 17/32 to 101 24/32, with an average of 101 18/32.

7. *August 12, 1935—\$100 million (additional) 2½-percent Treasury bonds of 1955-60*

Between July 31 and August 10 there was little demand for the longer issues, prices declining up to one-half point, although the short bonds were unchanged or only slightly easier. Apparently many of the 2½-percent Treasury bonds of 1955-60 received on the offering dated July 29 still remained on dealers' shelves. Following the announcement on August 12 of another issue of \$100 million of the 1955-60s, the market turned weak. There was some apprehension reflected in the market at this time as to both the frequency of offerings and the total amount intended to be raised by this method, and losses up 13/32ds were recorded by the general list. Moreover, as little buying interest was being shown in the market for the longest bonds, the market voiced objections to the additional offerings of 1955-60s, which was by far the largest Treasury issue outstanding and also the longest term. While the books were open, August 12-14, the price for the 1955-60s declined from 101 5/32 to 100 27/32. The average price of the bonds issued was 100 25/32. Total tenders of only \$147,264,000 were received, by far the smallest on any of the Treasury bond offerings.

During this period when the Treasury raised \$307 million through the three reopenings of this issue market weakness resulted in Treasury purchases in the market of \$74 million of the 2½s, or almost a quarter of the total.

8. *August 26, 1935—\$100 million (new series) 1½-percent Federal Farm Mortgage Corporation bonds of 1939*

Under unfavorable market conditions, prices having declined almost steadily for the preceding 3 weeks, \$100 million 1½-percent bonds of the Federal Farm Mortgage Corporation were offered on a tender basis on August 26. Weakness continued between August 26 and 28 while the books were open. The issue was not successful, only \$85,592,000 total tenders being received, of which \$85,172,000 were accepted. Prices of the accepted tenders ranged from 100 to 98, averaging 99, and affording an average yield of 1.762 percent. Comment in the press was to the effect that the coupon rate had been shaved too close. No comparable issue of farm mortgage bonds was outstanding at the time, although at market prices two Treasury note issues with 1939 maturities yielded approximately 1.30 percent, and the 1½-percent Home Owners Loan Corporation bonds of 1939 yielded 1.61 percent.

The new issue was quoted in the market at 99 13/32 bid on August 30 and advanced with the general market during the next few days to sell around 99 26/32. The balance of \$15 million, for which no tenders were received, was sold privately, through regular market channels, between October 8 to 14, at prices ranging from 100 to 100 2/32.

Secretary ANDERSON. We will certainly explore it further, sir.

Representative COFFIN. You end your statement by saying:

Improvements of the processes and mechanisms of the Government securities market will in no way solve our problems of fiscal imbalance—

with which I agree. But it is my feeling that you may have overstated your case when you went on to say:

Nor can they correct their problems of too much short-term public debt, of our need for continuous flexibility in our approach to monetary policies, of obtaining a volume of savings which will match our expanding investment needs, or of the cyclical instability of our financial market.

These things we have been talking about, the possibility of the Treasury purchasing securities; perhaps the possibility of auction—although the effect of that we would not know until we tried it; swapping; some of the reforms that you mentioned in your statement; possible margin regulations; repurchase agreements. Would not these things, although they may not bulk large, any one of them, these various mechanisms and processes, if successful, have a very definite effect on your ability to get out of too much of a short-range debt? Would they not help in giving you the power to achieve greater flexibility? Would they not help to some extent in fighting cyclical instability? And if you were successful in them, would they not also have an effect on savings available, which might then be put into the market, which are now kept out because of the violent fluctuations?

Secretary ANDERSON. Probably better terminology would have been if we had said that they cannot, within themselves, correct our problem. Anything which we can do to improve the market is an advantage, might very well help in distribution, might very well help in a number of ways.

The point we are making here, that I had in mind at the time of the statement, was that in certain market conditions at the moment, if we maintained the ceiling on the interest rate to which we can go for longer securities, we will still, by the very passage of time, have the maturities always shortened; that what we need to do, of course, was to have a greater flexibility in this regard.

Insofar as savings are concerned, if we can rid the country of a belief that we are going to have a continuous inflationary problem, then I think the volume of savings will rise.

Representative COFFIN. I agree that that is very important. But I think that the way your statement came out, you downgraded the use of all of these tools and mechanisms we have been talking about a little too much. I appreciate your candor in saying this.

Secretary ANDERSON. It was not intended to, and perhaps the grammar could have been better.

The CHAIRMAN. Congressman Widnall?

Representative WIDNALL. Secretary Anderson, there are presently pending in the Congress billions of dollars of new spending schemes. Conceivably, if Congress were to spend \$10 billion more than presently budgeted, what effect would that have on prices, credit, and interest rates, in your opinion, if there were a large excess of expenditures over budget receipts, and particularly so large that we could only go borrow the money?

Secretary ANDERSON. The extent to which we borrow the money would increase inflationary pressures. Some of the borrowings would undoubtedly come out of the hands of true savers, some of it out of the hands of banks, and some of it might very well be forced into the hands of the central bank. To the extent that you have to borrow from those types of institutions, you would build up inflationary pressures and increase costs.

Representative WIDNALL. You presently have a tightening money market, which is indicated by your difficulty in floating Government loans. Certainly additional spending would create additional pressures in bidding for services and in bidding for materials. Does that not inevitably cause inflation?

Secretary ANDERSON. It would cause increased price levels.

Representative WIDNALL. Increased prices?

Secretary ANDERSON. Yes.

Representative WIDNALL. You said in your statement:

Appropriate current governmental policy to promote growth must be consistent with long-range objectives and not resort to quick expedients that endanger sustainable development.

Do you have in mind particular matters when you say "quick expedients"? Do you have any particular programs that you would characterize as such?

Secretary ANDERSON. I am talking about such things as this. A year ago, when we were wrestling more with the problem of recession than inflation, there was a great deal of discussion in our country that perhaps, in order to restore a high level of business activity, we had to have very large tax reductions or very large expenditures, or some of both. It is my own judgment that had we at that time improvidently gone too far in either direction, we would now have a greater problem than we are currently confronting.

In any particular cycle in which we are, while there may be very honest differences of judgment and differences of opinion, all of which I respect, one in making up his own mind must say to himself, what do I accomplish by this technique today, and what is the long-range effect or impact if the economy moves in accordance with the way I believe that it will move?

I am simply trying to point out here that we must judge each of the fiscal or monetary instrumentalities of our Government, both with reference to its immediate and its long-range impact.

Representative WIDNALL. I notice, in attempting to analyze your statement, Secretary Anderson, that there seems to be quite an administration emphasis on research and development. In placing that emphasis, is it not with the thought that through that you create the job opportunities of the future, the employment of the future, rather than just a holding operation trying to maintain the status quo?

Secretary ANDERSON. No; what all of us want in this country is progress, and progress comes about to a large degree because of technological advances, because of our capacity to do new and different things and to utilize our resources more efficiently and more profitably.

Representative WIDNALL. Is not our growth materially affected by the many Government programs which we now have enacted that are just trying to maintain the status quo? I am thinking now about the farm subsidy program, and some of the activities of regulatory agencies, and trade restrictions. Is that not so, that our national growth is materially affected by those restrictions?

Secretary ANDERSON. Without referring to any specifics, historically people have a practice of developing a technique because of a particular set of circumstances. Then we are rather reluctant sometimes to review circumstances as they change, to see whether or not the policies which we adopted at a prior time in history are still valid.

It seems to me that progress is another way of saying that we must adapt ourselves to change. Change means whatever is desirable in order to bring about greater use of the human material resources of the country, out of which true growth is made.

Representative WIDNALL. With adaptability and flexibility, then, we can have more material growth than we have had in the past. We have had too many frictions encouraged to last too long.

Secretary ANDERSON. I think adaptability, flexibility, and willingness to make change, is a necessary ingredient.

Representative WIDNALL. Is the great rate of growth in the country materially affected by the emphasis on leisure, by the encouragement of more and more leisure? That is a tough question, I know. It provides recreational employment, I suppose. Is our national growth affected by some emphasis on leisure as against Russia's national growth?

Secretary ANDERSON. Let me say that if one tries to relate leisure time in this country to the philosophy of the Russians, if one should adopt a belief that the way in which you get a maximum growth in this country is to have a regulation of everybody's activities in everything that they do, then we are surrendering the very thing we are trying to preserve, and that is the freedom of our country.

There may be all shades of opinion as to whether or not people work long enough hours and that sort of thing, but when you finally get down to it, it is purely a question of whether or not we utilize to the best and most effective and efficient manner possible capacity of how many beings for making things out of the material resources of the Nation.

Leisure is a part of the human experience that we would not want to give up. On the other hand, the discipline of a free people requires that we, within ourselves and within our society, maintain some kind of reasonable balance between our periods of work and the times that we rest.

Representative WIDNALL. I just have one more question.

Our growth, too, I take it, is materially affected by the willingness of the private individual to save, and also by his willingness to pay increased taxes to meet the demands of the day. Are those not two things that should be emphasized?

Secretary ANDERSON. Certainly we have to have capital formation in real terms, and that comes out of savings. The extent to which we have to have tax money depends upon the needs of our country. If we could find a period in which we would have no fears of any kind, certainly it would be more desirable that we devote a larger portion of our national income to something other than the implements of defense, because the best use you can ever make of them is not to use them at all.

But on the other hand, we have to live with the fact that we have a period of force, in which there is probably going to be a continuation of tension. To that extent I would reiterate the philosophy I expressed to Senator Javits. It seems to me that then a country must say to itself, are we doing all we have to do, and as much that is desirable as we can afford to do at any given time?

Representative WIDNALL. Thank you, Mr. Secretary.

Representative REUSS. Mr. Secretary, I would like to button up our colloquy on the sense-of-Congress amendment.

I gather from your testimony that you favor what you call properly "flexibility," whereby the Federal Reserve should be encouraged to buy bills, certificates, notes, or bonds, as it deems wise, unfettered. That goes to the words "of varying maturity."

Your objection seems to boil down to the idea that there might be a depression, and that the Federal Reserve, if directed to increase the money supply by buying U.S. securities, might not be able to increase it fast enough.

Just sitting here, I have jotted down a proposed addition to that sense-of-Congress resolution as follows:

Provided, That if in a depression, the money supply cannot be expanded sufficiently rapidly by purchase of U.S. securities, the Federal Reserve should not consider itself confined to this method.

I would be very hopeful, Mr. Secretary, that you would agree that this additional language answers the one objection that you have been able to state. What I ask is that you think it over during the weekend, and let me know. If it does meet your objection, I will say right now I will be delighted to go to Mr. Mills, the chairman of the Ways and Means Committee, to Speaker Rayburn, and whoever, and give my view that that language in no way weakens the "sense" resolution, and that it does seem to meet your objection.

I hope you will think it over.

Secretary ANDERSON. Congressman, I will think it over, but may I say frankly I do not want to leave the impression that this is the sole problem which confronts me. It seems to me, one, that we are dealing here with the problem of debt management, that if the Congress is going to change the way in which the Federal Reserve System operates, it ought to be done by resorting to changes in the Federal Reserve Act, and that any attempt to change their modus operandi in a debt management bill raises this veiled worry about why do it in a debt management context.

Representative REUSS. If you could set forth the objection you gave this morning, plus the objection which you give now, that it should be in Federal Reserve legislation, and make it part of the record as soon as possible, it would be very helpful to all of us.

(The statement referred to is as follows:)

In judging the appropriateness of a "sense of Congress" action relating to the techniques of monetary policy, the single most important consideration involves the impact of such action on public confidence. Informed observers both at home and abroad are deeply concerned as to whether the action would be construed as working in the direction of restricting the ability of the Federal Reserve System to promote our vital economic objectives by pursuing flexible and appropriate monetary policies.

It is for this reason that I told the House Ways and Means Committee, when the Metcalf amendment was initially considered, that one of the most important factors to keep in mind was the interpretation of the meaning of the amendment on the part of responsible participants in financial markets, including investors in Government securities and all other fixed dollar obligations, foreign central banks, and everyone else who has an important stake in the soundness of the American economy.

According to the information we have received, the reactions in these quarters have been predominantly unfavorable. Concern has been expressed that flexibility in the administration of monetary policy would be impaired and that this, in turn, would raise doubts concerning the determination of the U.S. Government to pursue sound financial policies in the future.

The additional wording suggested by Congressman Reuss in these hearings would be aimed at making it clear that the System would be free to reduce member bank reserve requirements if it deemed necessary to combat recessionary tendencies in the economy. It is my judgment that the addition of such language would not be sufficient to allay the fears already expressed concerning the implications of the amendment.

Part of the concern over the implications of the Metcalf amendment stems, I think, from uncertainty as to whether the amendment is permissive or mandatory. In view of the fact that the Federal Reserve System is directly responsible to Congress, it is not surprising that a number of observers view the amendment, if not as a directive, as a strong congressional presumption relating to the manner in which the instruments of monetary policy are to be utilized.

There is, of course, no doubt about the authority of the Congress to issue specific directives to the Federal Reserve System. The important question, however, relates to the nature of such directives: whether they should pertain to the actual use of credit control instruments, or whether they should be broader in nature. In this connection, I would respectfully call the committee's attention to the conclusions of your Subcommittee on Monetary, Credit, and Fiscal Policies in 1950:

"It appears to us impossible to prescribe by legislation highly specific rules to guide the determination of monetary and debt management policies, for it is impossible to foresee all situations that may arise in the future. The wisest course for Congress to follow in this case is to lay down general objectives, to indicate the general order of importance to be attached to these various objectives, and to leave more specific decisions and actions to the judgment of the monetary and debt management officials. * * *" (pp. 27 and 28 of subcommittee report).

This conclusion, which was reached after a thorough and comprehensive study of monetary, credit, and fiscal policies, seems as valid today as in 1950.

Moreover, the legislation pending before the House Ways and Means Committee relates primarily to debt management. If, within the context of this type of legislation, there are amendments that would normally pertain to the Federal Reserve Act, additional doubts may be generated as to the reasons underlying the amendments. Such doubts can contribute to instability in financial markets.

In view of the fact that concern over the Metcalf amendment stems not just from the language, but from several more basic considerations, I do not believe that the additional language suggested by Congressman Reuss would in itself be sufficient to allay the fears that have been expressed concerning the implications of the amendment.

If the Metcalf amendment, or the suggested changes in language in it, has no meaning, there is no reason for it. If it has meaning, we must be concerned about it.

Secretary ANDERSON. May I say again that I feel a primary obligation to make these statements to the House Ways and Means Committee, but to the extent that I can do so, I would be glad to elaborate upon it.

Representative REUSS. Thank you, Mr. Chairman.

The CHAIRMAN. Mr. Reuss, I do not want to project myself unduly into this discussion, but perhaps we could remove some of the mental doubts and uncertainties of the Secretary by having this resolution that was passed out, not merely a new resolution, but an amendment to the Federal Reserve Act, and therefore this would meet your technical objection that it should be considered as a part of the Federal Reserve Act.

I understand that Congressman Curtis wants to make some comment on Congressman Reuss' statement.

Representative CURTIS. Yes, and I want to ask permission to make it while you are still here. It is a very limited statement.

In regard to this so-called Reuss amendment, the attitude of myself and many of us is that if we can cut the thing down to where it says nothing, then we will go along with it. But if it means anything, we are opposed to it. The question that worries us now is that it might be interpreted to say something.

Representative REUSS. It surely does mean something.

Representative CURTIS. Our opinion is that probably it does not say anything, and if that is so, we are not too concerned. But essentially,

I would say that it surprises me that the gentleman from Wisconsin, being a member of the Banking and Currency Committee, would want to give to the Ways and Means Committee this jurisdiction. Frankly, we do not want it. We would prefer to deal with that debt management as best we can and leave to Banking and Currency the question of amending the Federal Reserve Act.

Representative REUSS. I was just trying to be helpful.

Representative PATMAN. Mr. Chairman, may I comment briefly on what Mr. Curtis said?

I can see why Mr. Martin does not want this language. A number of times before this committee, one time in particular in 1954, Mr. Wolcott was chairman of the Joint Economic Committee, and something was said about the relationship between Congress and the Federal Reserve. Mr. Martin said that we were the servants of Congress, and Mr. Wolcott said, "Well, let us consider, instead of the master and servant relationship, it is a principal and agent." And we discussed it from that standpoint.

Therefore, bearing in mind what he actually believes in relationship here to the sense of Congress, the words "sense of Congress" would obligate him just as much as if we were to enact it into law. I think that is the reason he does not want this sense-of-Congress resolution.

Senator BUSH. Do you bear with the sense-of-Congress resolution rather than enacting legislation?

Representative PATMAN. I will take it any way you can get it. And right now I think the best answer to the Ways and Means is that I am perfectly willing for our committee to give them the jurisdiction.

Representative CURTIS. The whole jurisdiction?

Representative PATMAN. Of the "sense" resolution.

Representative CURTIS. How about our taking the Federal Reserve Act into our jurisdiction?

Representative PATMAN. If you will do more about it than we are doing.

The CHAIRMAN. Mr. Secretary, the questions which have come from the Democratic side of this table I think clearly indicate that what we want is more competition in the Government bond market instead of less, as we have sometimes been charged with favoring. The questioning of the Congressman from Texas, and Congressman Reuss and Congressman Coffin was all directed at having a more competitive bond market. This, I think, needs to be emphasized.

Now, it is true, is it not, that before any appreciable bond issue is floated by the Treasury, the Treasury recalls in advisory committees from the American Banking Association and the Investment Bankers Association, and upon occasion from the mutual savings banks and from insurance companies?

Secretary ANDERSON. That is correct, and on occasion from the savings and loan institutions.

The CHAIRMAN. Yes.

And some of the mechanism of these operations is described in the hearings of the subcommittee of the House Committee on Government Operations, held in 1956. I have gone over those hearings very, very carefully, and I think the following statement is correct. I am going to take the record of the American Bankers Association as the type, because it is more carefully kept and more fully recorded.

The committee selected by the president of the American Bankers Association meets at the Treasury. Problems of the Treasury are outlined to it. The advisory committee then meets by itself and comes in with a recommendation. The Secretary of the Treasury, or the Under Secretary acting for him, then appears, does not make a definite commitment, but states that he will take the opinions under consideration. Advice is generally solicited from the Investment Bankers Association at the same time as from the American Bankers Association, and sometimes from these other groups.

Is this not a substantially accurate record as to what happens?

Secretary ANDERSON. Substantially, yes, sir.

The CHAIRMAN. On pages 12 to 16 of the House hearings to which I have referred, the American Bankers Association furnished for the record the accounts for each date of hearings, consisting first of the problem of financing which they faced, the committee recommendations, and then the Treasury decision.

I have tabulated those recommendations and decisions. I find that in the year 1952, the Treasury accepted the exact advice of the American Bankers Association on 11 occasions, that in one instance they accepted the advice with only minor changes. In seven cases they rejected the advice. Or, if I can divide, this means that the advice was rejected in 37 percent of the cases.

In the 3 years from March 20, 1953, to February 29, 1956, the Treasury accepted the advice of the American Bankers Association in 24 cases, in 9 cases accepted the advice with only very minor modification, in 3 cases accepted the advice with major changes, and in 5 cases rejected the advice.

With each meeting, I think I should say, there were several recommendations, and we are taking the total recommendations.

Again, if I can divide, since 6 recommendations of 45 were rejected, this comes to 12 percent instead of the 37 percent rejected in the year 1952.

In view of the fact that the ultimate decision of the Treasury in such an overwhelming proportion of the cases could coincide with the recommendations of the American Bankers Association, can it be said that the rates and terms which you fix are truly competitive, or would not a better term be that they are collectively bargained rates or negotiated rates? And if I may make this illustration more vivid, suppose that we have a country X—and I am not referring to any one country, so I hope there will be no international or internal implications in what I say. Suppose you have a country X which has a labor government, and that this labor government employs a third of the people; that the secretary of labor fixes the basic wage rate periodically, and before he fixes a wage rate or decides what the competitive wage rate is, he calls upon the equivalent of Mr. Meany or Mr. Reuther or Mr. George Harrison to send a committee up and advise him; and they advise him that the wage rate should be increased, let us say, by 9 cents an hour; and upon due consideration, after taking this advice, in from 63 to 88 percent of the cases, the secretary of labor decides that wages should be increased by 9 cents an hour.

Under those conditions, could it be said that the wage rate fixed by the government was a competitive rate, or would it not be a negotiated rate, or a collectively bargained rate?

I think every financial reporter in the United States would spew out the idea that this was a competitive rate of wages.

While I address this question not to them but to you, I would like to ask you how you can say that it is a competitively determined rate when this was arrived at after taking into account the opinions of the American Bankers Association, the Investment Bankers Association and, so far as our records show, coming to an agreement in approximately 80 percent of the cases.

May I say I am going to ask the staff to request from the American Bankers Association, because I understand the Treasury does not keep a record of these things, some material from the conferences from the 29th of February until the present date. (See pp. 1225-1230.)

That is a rather heavy broadside that I shot at you, but it is crucial, and I think it goes to the heart of the subject. It is dictated by the desire of those of us on this side of the table, at least, to have a competitive money market.

Senator BUSH. Senator, would you yield right there?

The CHAIRMAN. I have no imputations as to what anyone else believes. I am merely summarizing the opinions of those of us on this side.

Senator BUSH. I just wondered whether the Senator, as long as he has all those dates of meetings, had the results of how far the issues were oversubscribed or undersubscribed in these particular things? That might also indicate whether a correct decision has been made.

The CHAIRMAN. I think they are nearly always oversubscribed. Senator Bush, I do not have the huge resources which either the Treasury or the Republican National Committee has. We sacrificed some hours of sleep to get these done.

Senator BUSH. How about the Democratic National Committee?

The CHAIRMAN. We are very much undermanned.

Now, Mr. Secretary, this is a potent question I have addressed to you, concerning whether this is a negotiated or collectively bargained rate, rather than the competitive rate it was described to be by Mr. Humphrey in his egg analogy. I do not accuse him of being an egghead, however.

Secretary ANDERSON. The practices to which the Senator referred were inaugurated, according to my information, by Secretary Morgenthau a good many years ago.

The CHAIRMAN. Yes, in wartime; and in wartime this is necessary.

Senator BUSH. There is a cold war now.

Secretary ANDERSON. These committees are selected without any consultation on the part of the Treasury by the respective organizations.

The CHAIRMAN. Let me say to you that if Mr. Meany ever sent a committee out, his secretary of labor would not dictate who comprised his committee. Mr. Meany would select the committee.

Secretary ANDERSON. Each of these committees is given, as the Senator stated, various information with reference to a particular financing problem which may be imminent, and sometimes information concerning problems which we face a month or so ahead. This is not any information which is not otherwise available to the market. They are not given any special information. It is merely a summation of factors.

Prior to any meeting of this group, the financial analysts and writers in the country are fully aware of the kinds of problems which the Treasury faces, and they make their own analysis all across the country. When one is given a stated problem in financing, in most instances there is not a great deal of room for various differences of judgment. There is a common body of knowledge, particularly among the people who constantly deal in financial matters, which would lead to relatively close matters of judgment.

In the case of the Treasury, the staff of the Treasury works in a very concentrated way on these problems before the meetings. We also get any ideas the Federal Reserve people have. We have many discussions. Sometimes the conclusions that we arrive at before any of the meetings are held coincide with the kind of judgments that we receive. Sometimes they do not. We do not advise them of that.

The CHAIRMAN. Mr. Secretary, we do not have the record since February 29, 1956, but the record prior to that time indicated that after March 1953, in the overwhelming proportion of the cases, the final decision did agree with the recommendation.

Secretary ANDERSON. That doesn't mean we accepted their advice. It is not a question of negotiation. It is merely a reflection of the fact that with a given market problem, there was not too much difference in judgment about it.

Frankly, the thing we are most concerned about is not the exact rates, although at times we may arrive at the same conclusions, but rather getting judgments as to the existence of markets for various types and kinds of securities—how much can be sold in what maturity area, and so forth.

We therefore try to take into consideration not just the kind of counsel which would come from those committees, but the kind of counsel which we would gather from a great many other market analysts, from all of the data which we have at hand, and from a continuous group of conversations that go on day after day with people who express some interest in various kinds of markets that exist in the country.

The final judgment in these things, although it may at times coincide with some judgments which we have given, nevertheless is finally determined only by the Treasury.

If we did not get an oversubscription to these securities, I think generally it would be regarded in the market as a failure.

The CHAIRMAN. I brought in this question of oversubscription merely to meet the objection of the Senator from Connecticut.

Secretary ANDERSON. Yes.

Senator BUSH. You did not bring in the information I asked for, though.

The CHAIRMAN. Well, that could be supplied.

By the way, can the Treasury supply for the Senator from Connecticut and the Senator from Illinois the record as to the degree to which these issues have or have not been oversubscribed?

Secretary ANDERSON. Oh, yes.

Senator BUSH. And the extent of it.

The CHAIRMAN. I think the record will show that they have almost invariably been oversubscribed in very large amounts.

Senator BUSH. That would be, as the Senator said, the normal thing to expect; else it would be greeted with failure.

(The material requested is as follows:)

The attached table 4 from the June 1959 Treasury bulletin presents data on total subscriptions and amounts issued on all Treasury offerings of marketable securities (other than regular weekly Treasury bills) from 1953 to date. Table 4 indicates that the amount of cash subscriptions for new Treasury certificates, notes, and bonds has varied from $1\frac{1}{2}$ times the amount issued, to slightly more than seven times the amount issued, with an average of three times. All subscriptions received in an exchange offering are, of course, allotted in full.

The extent of oversubscription to a new Treasury issue does not necessarily measure the market's appraisal of the attractiveness of the terms of that issue. The extent of oversubscription merely indicates the sum of all the guesses by buyers as to what total subscriptions might be.

Oversubscriptions to Treasury cash issues are expected by those who buy and have been a common occurrence for many years. In the 8 years 1933-40, for example, subscriptions ran from $1\frac{1}{2}$ times allotments to 38 times, with an average for the entire period of about 7 times. In each cash financing the Treasury always announces in advance the approximate size of each new issue which it is offering. This is a decision which is arrived at only after a careful nationwide survey of approximate investor demand for various alternative types of offering. The Treasury always announces the approximate size of the offering (subject to customary overallotment of up to 10 percent or so) so that investors will make their decisions in full knowledge of the size of the total supply being placed on the market.

If a potential buyer wants \$1 million of a new issue, for example, and the general discussion in the market indicates to him that he would guess there might be four times as many subscriptions as actual allotments (that probably only about 25 percent of total subscriptions will be allotted) he may then enter his subscription for \$4 million. He would prefer to buy his \$1 million of new bonds directly from the Treasury so he is willing to bid for more than a million dollars to make sure. He knows that he can always make up any deficiency by buying more of the bonds in the open market later on, but if the issue is attractive he reasons that he can probably do so only by paying a premium which, of course, would lessen the attractiveness of the security to him. He knows also that if it turns out he subscribes to too many bonds, and that is true of other investors, he may have to sell the excess at a loss, so he wants to base his subscription on the best possible guess as to what the actual results of the offering will be. He would be the most surprised man in the world if the Treasury decided to accept his subscription in full.

The Treasury prices its new issues so that they are slightly more attractive to an investor than the return he would get if he bought an outstanding issue in the market at the same time. The margin between an interest yield that attracts buyers and results in a heavy oversubscription on a given day as against a yield that might cause the issue to fail, in terms of being fully subscribed, is very narrow. It is the market price behavior, therefore, of a new Treasury issue once it is available for trading which is the most important gauge of whether it is attractive to investors or not, once it has been determined that subscriptions have been received at least equal to the amount being offered. Market price behavior can, in turn, be measured in two ways—with reference to its own issue price, and with reference to the market trend of outstanding issues of comparable maturity.

There are many cases in recent years where heavily oversubscribed issues have fallen below par when first quoted in the market. One example was the Treasury's cash offering in September 1957 of approximately $\$1\frac{1}{2}$ billion to the public of 12-year 4 percent bonds. The amount of subscriptions tendered for these bonds was $\$4\frac{1}{2}$ billion, yet the issue was quoted at only a small premium immediately after the subscription books were closed and fell below par within a few days. In the market environment of the time any sustained demand for more than $\$1\frac{1}{2}$ billion of these securities would not have depressed the price in this way. Actually, in this case, enough purchasers expected an even lower allotment percentage and received more bonds than they expected to. The resulting sales in the market pushed the price down. Small subscribers, of course, are protected by the Treasury so that they always get full allotment (in this particular case subscriptions up to \$50,000 were allotted in full).

The size of oversubscription in the case of a bill auction—as compared with certificates, notes, and bonds where the Treasury fixes the price—can also be deceptive if a large number of bids are submitted at very low prices on the chance that they might possibly be accepted, in which case a quick profit could be realized by dumping them in the secondary market.

The extent of oversubscription on Treasury bill issues has also varied widely. Data on tax anticipation bills and other bills outside the regular weekly series are also contained in the attached table 4. They reveal a variation in ratio of subscriptions (tenders) to accepted bids ranging from bare coverage (1.1 times) to about $3\frac{1}{4}$ times.

Data on weekly bill auctions are shown for recent months in the attached table 2, also taken from the June 1959 Treasury Bulletin. The ratio of subscriptions to accepted bids in the shorter bills shown in the table varied from a little less than $1\frac{1}{2}$ times to about $2\frac{1}{2}$ times.

PUBLIC DEBT OPERATIONS

TABLE 4.—Offerings of public marketable securities other than regular weekly Treasury bills

[Dollars in millions]

Date sub- scription books opened or bill tenders received	Date of issue	Description of security ¹	Period to final maturity (years, months, days) ²	Amount of sub- scriptions tendered		Amount issued		Allot- ment ratio
				Cash ³	Ex- change	For cash ⁴	In ex- change ⁴	
Feb. 2, 1953	Feb. 15, 1953	2½-percent certificate, Feb. 15, 1954 A	1 year		\$8, 114		\$8, 114	100
	do	2½-percent bond, Dec. 15, 1958	5 years 10 months		620		620	
(⁵)	Apr. 1, 1953	1½-percent note, Apr. 1, 1958 EA	5 years		393		393	100
Apr. 13, 1953	May 1, 1953	3¼-percent bond, June 15, 1978 B3	30 years 1½ months	\$5, 250	\$ 418	\$1, 188	\$ 418	
May 20, 1953	June 1, 1953	2½-percent certificate, June 1, 1954 B	1 year		4, 858		4, 858	100
May 29, 1953	June 3, 1953	2.383-percent bill, Sept. 18, 1953, tax anticipation ⁶ (at auction)	107 days	1, 876		800		
July 6, 1953	July 15, 1953	2½-percent certificate, Mar. 22, 1954 C, tax anticipation ⁶	8 months	8, 687		5, 902	2, 788	(10)
Aug. 5, 1953	Aug. 15, 1953	2½-percent certificate, Aug. 15, 1954 D	1 year		2, 788		2, 788	
Sept. 2, 1953	Sept. 15, 1953	2½-percent certificate, Sept. 15, 1954 E	1 year		4, 724		4, 724	100
	do	2½-percent note, Mar. 15, 1957 A	3 years 6 months		2, 997		2, 997	
(⁵)	Oct. 1, 1953	1½-percent note, Oct. 1, 1958 EO	5 years		121		121	100
Oct. 28, 1953	Nov. 9, 1953	2½-percent bond, Sept. 15, 1961	7 years 10 months	12, 543		2, 239		
Nov. 18, 1953	Dec. 1, 1953	1½-percent note, Dec. 15, 1954 B	1 year ½ month		8, 175		8, 175	(11)
	Feb. 15, 1953	2½-percent bond, Dec. 15, 1958, reopening	5 years ½ month		1, 748		1, 748	
Feb. 1, 1954	Feb. 15, 1954	1½-percent certificate, Feb. 15, 1955 A	1 year		7, 007		7, 007	100
	do	2½-percent bond, Nov. 15, 1961	7 years 9 months		11, 177		11, 177	
Mar. 16, 1954	Mar. 22, 1954	0.956-percent bill, June 24, 1954, tax anticipation ⁶ (at auction)	94 days	2, 717		1, 501		100
Apr. 21, 1954	Apr. 27, 1954	0.726-percent bill, June 18, 1954, tax anticipation ⁶ (at auction)	52 days	2, 987		1, 001		
(⁵)	Apr. 1, 1954	1½-percent note, Apr. 1, 1959 EA	5 years		119		119	100
May 4, 1954	May 17, 1954	1½-percent note, Feb. 15, 1959 A	4 years 9 months	9, 760		2, 205		
May 5, 1954	do	do	do		2, 897		2, 897	(12)
	do	1½-percent certificate, May 17, 1955 B	1 year		3, 886		3, 886	
July 21, 1954	Aug. 2, 1954	1-percent certificate, Mar. 22, 1955 C, tax anticipation ⁶	7½ months	9, 250		3, 734		(13)
Aug. 3, 1954	Aug. 15, 1954	1½-percent certificate, Aug. 16, 1955 D	1 year		3, 558		3, 558	
	do	2½-percent bond, Nov. 15, 1960	6 years 3 months		3, 806		3, 806	100
Sept. 23, 1954	Oct. 4, 1954	1½-percent note, May 15, 1957 B	2 years 7½ months	8, 190		4, 155		
(⁵)	Oct. 1, 1954	1½-percent note, Oct. 1, 1959 EO	5 years		99		99	100
Nov. 22, 1954	Aug. 15, 1954	1½-percent certificate, Aug. 15, 1955 D, reopening	8 months		4, 919		4, 919	
	Dec. 15, 1954	1½-percent certificate, Dec. 15, 1955 E	1 year		5, 359		5, 359	100
Feb. 1, 1955	do	2½-percent bond, Aug. 15, 1963	8 years 8 months		6, 755		6, 755	
	do	1½-percent note, Mar. 15, 1956 A	1 year, 1 month		8, 472		8, 472	100
	do	2-percent note, Aug. 15, 1957 C	2 years, 6 months		3, 792		3, 792	
	do	3-percent bond, Feb. 15, 1965	40 years		1, 924		1, 924	(14)
Mar. 22, 1955	Apr. 1, 1955	1½-percent certificate, June 22, 1955 F, tax anticipation ⁶	2½ months	7, 938		3, 210		
(⁵)	do	1½-percent note, Apr. 1, 1960 EA	5 years		198		198	

See footnotes at end of table.

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TABLE 4.—Offerings of public marketable securities other than regular weekly Treasury bills—Continued

Date subscription books opened or bill tenders received	Date of issue	Description of security ¹	Period to final maturity (years, months, days) ²	Amount of subscriptions tendered		Amount issued		Allotment ratio
				Cash ³	Ex-change	For cash ³	In exchange ⁴	
May 3, 1955	May 17, 1955	2-percent note, Aug. 15, 1956 B	1 year, 3 months	3,989	3,174	2,532	3,174	(15)
July 8, 1955	July 18, 1955	1½-percent certificate, Mar. 22, 1956 A, tax anticipation ⁵	8 months	10,620		2,202		(16)
July 11, 1955	Feb. 15, 1955	3-percent bond, Feb. 15, 1955, reopening	39 years, 7 months	1,720		821		(17)
July 20, 1955	Aug. 1, 1955	2-percent certificate, June 22, 1956 B, tax anticipation ⁵	10½ months		1,486		1,486	100
	May 17, 1955	2-percent note, Aug. 15, 1956 B, reopening	1 year		6,841		6,841	
Oct. 3, 1955	Oct. 11, 1955	2½-percent certificate, June 22, 1956 C, tax anticipation ⁵	8 months	8,778		2,970		(18)
(5)	Oct. 1, 1955	1½-percent note, Oct. 1, 1960 EO	5 years		278		278	100
Nov. 28, 1955	Dec. 1, 1955	2½-percent certificate, Dec. 1, 1956 D	1 year		9,083		9,083	100
	do.	2½-percent note, June 15, 1958 A	2 years, 6 months		2,283		2,283	
Dec. 8, 1955	Dec. 15, 1955	2.46-percent bill, Mar. 23, 1956, tax anticipation ⁵ (at auction)	99 days	4,130		1,501		100
Mar. 5, 1956	Mar. 5, 1956	2½-percent certificate, Feb. 15, 1957 A	11½ months		7,219		7,219	
	Dec. 1, 1955	2½-percent note, June 15, 1958 A, reopening	2 years, 3 months		2,109		2,109	100
(9)	Apr. 1, 1956	1½-percent note, Apr. 1, 1961 EA	5 years		144		144	100
July 16, 1956	July 16, 1956	2½-percent note, Aug. 1, 1957 D	1 year, ½ month		12,056		12,056	100
Aug. 6, 1956	Aug. 15, 1956	2½-percent certificate, Mar. 22, 1957 B, tax anticipation ⁵	7 months	10,613		3,221		(19)
(9)	Oct. 1, 1956	1½-percent note, Oct. 1, 1961 EO	5 years		332		332	100
Oct. 10, 1956	Oct. 17, 1956	2.627-percent bill, Jan. 16, 1957, special (at auction)	91 days	4,761		1,603		100
Nov. 13, 1956	Nov. 16, 1956	2.617-percent bill, Feb. 15, 1957, special (at auction)	do	4,637		1,750		
Nov. 19, 1956	Dec. 1, 1956	3¼-percent certificate, June 24, 1957 C, tax anticipation ⁵	6½ months		1,312		1,312	100
	do.	3¼-percent certificate, Oct. 1, 1957 D	10 months		7,271		7,271	
Dec. 12, 1956	Dec. 17, 1956	2.58-percent bill, Mar. 22, 1957, tax anticipation ⁵ (at auction)	95 days	3,786		1,006		100
Jan. 11, 1957	Jan. 16, 1957	3.305-percent bill, June 24, 1957, tax anticipation ⁵ (at auction)	159 days	2,414		²⁰ 1,601		
Feb. 4, 1957	Feb. 15, 1957	3¾-percent certificate, February 14, 1958 A	1 year		8,414		8,414	100
	do.	3½-percent note, May 15, 1960 A	3 years 3 months		1,464		1,464	
Feb. 7, 1957	do.	3.231-percent bill, June 24, 1957, tax anticipation ⁵ (at auction)	129 days	2,302		²⁰ 1,750		100
Mar. 18, 1957	do.	3¾-percent certificate, Feb. 14, 1958 A, reopening	10½ months	7,489		2,437		
(9)	do.	3½-percent note, May 15, 1960 A, reopening	3 years 1½ months	5,868		942		(21)
	Apr. 1, 1957	1½-percent note, Apr. 1, 1962 EA	5 years		551		551	100
May 6, 1957	May 1, 1957	3½-percent certificate, Apr. 15, 1958 B	1½ months		2,351		2,351	100
	do.	3½-percent note, Feb. 15, 1962 A	4 years 9½ months		647		647	
May 22, 1957	May 27, 1957	2.825-percent bill, Sept. 23, 1957, tax anticipation ⁵ (at auction)	119 days	3,689		1,501		100
June 26, 1957	July 3, 1957	3.485-percent bill, Mar. 24, 1958, tax anticipation ⁵ (at auction)	264 days	4,547		3,002		
July 22, 1957	Aug. 1, 1957	3¾-percent certificate, Dec. 1, 1957 E	4 months	100	9,871	100	9,871	100
	do.	4-percent certificate, Aug. 1, 1958 C	1 year	100	10,487	100	10,487	
	do.	4-percent note, Aug. 1, 1961 A ²²	4 years	100	2,509	100	2,509	

Aug. 14, 1957	Aug. 21, 1957	4.173-percent bill, Apr. 1, 1958 special (at auction).....	237 days.....	3,178		1,751			
Sept. 16, 1957	Aug. 1, 1957	4-percent certificate, Aug. 1, 1958 C, reopening.....	10 months.....	3,067		933			
	Sept. 26, 1957	4-percent note, Aug. 15, 1962 B ²¹	4 years 11 months.....	6,121		2,000			(²³)
	Oct. 1, 1957	4-percent bond, Oct. 1, 1969.....	5 years.....	4,648		657			(²⁴)
(⁴)	do.....	1½-percent note, Oct. 1, 1962 E O.....	5 years.....		590		590		100
Nov. 20, 1957	Nov. 29, 1957	3¼-percent note, Nov. 15, 1962 C.....	4 years 11½ months.....	7,786		1,143			(²⁷)
	Dec. 2, 1957	3½-percent bond, Nov. 15, 1974.....	16 years 11½ months.....	3,817		654			(²⁸)
Nov. 21, 1957	Dec. 1, 1957	3½-percent certificate, Dec. 1, 1958 D.....	1 year.....		9,833		9,833		100
Feb. 3, 1958	Feb. 14, 1958	2½-percent certificate, Feb. 14, 1959 A.....	do.....		9,770		9,770		
	do.....	3-percent bond, Feb. 15, 1964.....	6 years.....		3,854		3,854		100
	do.....	3½-percent bond, Feb. 15, 1990.....	32 years.....		1,727		1,727		
Feb. 28, 1958	Feb. 28, 1958	3-percent bond, Aug. 15, 1966.....	8 years 5½ months.....	6,715		1,484			(²⁹)
(⁵)	Apr. 1, 1958	1½-percent note, Apr. 1, 1963 E A.....	5 years.....		533		533		100
Apr. 7, 1958	Apr. 15, 1958	2½-percent note, Feb. 15, 1963 A.....	4 years 10 months.....	15,741		3,971			(³⁰)
June 3, 1958	June 3, 1958	3¼-percent bond, May 15, 1985, issued at 100¼.....	26 years 11 months.....	2,570		1,135			(³¹)
June 4, 1958	June 15, 1958	1½-percent certificate, May 15, 1959 B.....	11 months.....		1,817		1,817		100
	do.....	2½-percent bond, Feb. 15, 1965.....	6 years 8 months.....		7,388		7,388		
July 21, 1958	Aug. 1, 1958	1½-percent certificate, Aug. 1, 1959 C.....	1 year.....		13,500		13,500		100
July 29, 1958	Aug. 6, 1958	1½-percent certificate, Mar. 24, 1959 D, tax anticipation ⁶	8 months.....	5,962		3,567			(³²)
(⁶)	Oct. 1, 1958	1½-percent note, Oct. 1, 1963 E O.....	5 years.....		506		506		100
Sept. 29, 1958	Oct. 10, 1958	3½-percent note, Nov. 15, 1959 B.....	1 year 1 month.....	2,686		1,184			
	Oct. 8, 1958	3¼-percent bill, May 15, 1959, issued at 98.023 (special at fixed price).....	219 days.....	5,805		2,735			(³³)
Nov. 14, 1958	Nov. 20, 1958	2.999-percent bill, June 22, 1959, tax anticipation ⁸ (at auction).....	214 days.....	5,950		2,907			
Nov. 19, 1958	Dec. 1, 1958	3¼-percent certificate, Nov. 15, 1959 E, issued at 99.95.....	11¼ months.....		7,711		7,711		100
	do.....	3½-percent note, May 15, 1961 B, issued at 99¼.....	2 years 5½ months.....		4,078		4,078		
Jan. 12, 1959	Jan. 21, 1959	3¼-percent note, May 15, 1960 B, issued at 99¾.....	1 year 4 months.....	5,508		2,738			(³⁴)
	Jan. 23, 1959	4-percent bond, Feb. 15, 1980, issued at 99.00.....	21 years 1 month.....	²² 1,800		²³ 884			(³⁵)
Feb. 2, 1959	Feb. 15, 1959	3¼-percent certificate, Feb. 15, 1960 A, issued at 99.993.....	1 year.....		11,363		11,363		100
	do.....	4-percent note, Feb. 15, 1962 D, issued at 99.993.....	3 years.....		1,435		1,435		
Feb. 11, 1959	Feb. 16, 1959	3.293-percent bill, Sept. 21, 1959, tax anticipation ⁹ (at auction).....	217 days.....	2,984		1,502			

See footnotes at end of table.

TABLE 4.—Offerings of public marketable securities other than regular weekly Treasury bills—Continued

Date subscription books opened or bill tenders received	Date of issue	Description of security ¹	Period to final maturity (years, months, days) ²	Amount of subscriptions tendered		Amount issued		Allotment ratio
				Cash ³	Ex-change	For cash ³	In ex-change ⁴	
Mar. 23, 1959	Apr. 1, 1959	4-percent note, May 15, 1963 B	4 years 1½ months	\$ ³ 3,052		\$ ³ 1,743		(*)
(5)	Oct. 1, 1957	4-percent bond, Oct. 1, 1969, reopening	10 years 6 months	\$ ³ 1,502		\$ ³ 619		(35)
	Apr. 1, 1959	1½-percent note, Apr. 1, 1964 EA	5 year		20		20	100
Mar. 26, 1959	do	3.386-percent bill, Jan. 15, 1960, special (at auction)	289 days	3,445		2,006		
May 6, 1959	May 11, 1959	3.835-percent bill, Apr. 15, 1960, special (at auction)	340 days	3,461		2,003		
May 7, 1959	May 15, 1959	3.565-percent bill, Dec. 22, 1959, tax anticipation ⁴ (at auction)	221 days	\$ ³ 1,699		\$ ³ 1,500		
May 11, 1959	do	4-percent certificate, May 15, 1960 B, issued at 99.95	1 year		\$ ³ 1,269		\$ ³ 1,269	100

¹ Issued at par except as noted. For bill issues sold at auction, the rate shown is the equivalent average rate (bank discount basis) on accepted bids. For details of bill offerings, see table 2. In reopenings, the amount issued is in addition to the amount in original offering.

² From date of additional issue in case of a reopening.

³ Consists of all public cash subscriptions and subscriptions by U.S. Government investment accounts.

⁴ For maturing securities exchanged for the new issues, see table 6.

⁵ Exchange offering available to owners of nonmarketable 2¾ percent Treasury bonds, investment series B-1975-80, dated Apr. 1, 1951. For further information on the original offering see "Treasury Bulletin" for Apr. 1951, p. A-1. Amounts shown are as of May 31, 1959.

⁶ The bond offering was made available for exchange of series F and G savings bonds maturing from May 1 through Dec. 31, 1953.

⁷ Total allotments on cash subscriptions were limited to approximately \$1,000,000,000. Nonbank subscriptions in amounts up to and including \$5,000 were allotted in full. All other subscriptions were allotted 20 percent. Commercial banks' subscriptions were restricted to an amount not exceeding 5 percent of their time deposits as of Dec. 31, 1952. The Treasury also reserved the right to allot limited amounts of these bonds to Government investment accounts, which subscribed to a total amount of \$118,000,000. Payment for the bonds allotted could be made with accrued interest at any time not later than July 31, 1953.

⁸ Tax anticipation bill, acceptable at face value in payment of income and profits taxes due on the quarterly payment date immediately preceding maturity.

⁹ Tax anticipation certificates, acceptable at par plus accrued interest to maturity in payment of income and profits taxes due on the quarterly payment date immediately preceding maturity.

¹⁰ Subscriptions for amounts up to and including \$100,000 were allotted in full. Subscriptions for amounts over \$100,000 were allotted 67 percent but in no case less than \$100,000.

¹¹ Subscriptions for amounts up to and including \$10,000 were allotted in full. Subscriptions from mutual savings banks, insurance companies, pension and retirement funds, and State and local governments were allotted 24 percent. All others, including

commercial banks, were allotted 16 percent but not less than \$10,000 on any 1 subscription.

¹² Subscriptions for amounts up to and including \$10,000 were allotted in full. All other subscriptions were allotted 22 percent but in no case less than \$10,000.

¹³ Subscriptions for amounts up to and including \$50,000 were allotted in full. Subscriptions for amounts over \$50,000 were allotted 40 percent but in no case less than \$50,000.

¹⁴ Subscriptions for amounts up to and including \$50,000 were allotted in full. Subscriptions for amounts over \$50,000 were allotted 50 percent but in no case less than \$50,000.

¹⁵ Cash subscriptions for \$100,000 or less were allotted in full. Subscriptions for more than \$100,000 were allotted 62 percent but in no case less than \$100,000.

¹⁶ Subscriptions for \$100,000 or less were allotted in full. Subscriptions for more than \$100,000 were allotted 19 percent but in no case less than \$100,000.

¹⁷ Subscriptions from savings-type investors totaled \$749,000,000 and were allotted 65 percent. Subscriptions from all other investors totaled \$970,000,000 and were allotted 30 percent. Subscriptions for \$25,000 or less were allotted in full. Subscriptions for more than \$25,000 were allotted not less than \$25,000. In addition to the amount allotted to the public, \$25,000,000 of the bonds were allotted to Government investment accounts. Savings-type investors were given the privilege of deferring payment for the bonds, provided that not less than 25 percent of the bonds allotted were paid for by July 20, 1955, not less than 60 percent by Sept. 1, 1955, and full payment by Oct. 3, 1955.

¹⁸ Subscriptions for \$100,000 or less were allotted in full. Subscriptions for more than \$100,000 were allotted 32 percent but in no case less than \$100,000.

¹⁹ Subscriptions for \$100,000 or less were allotted in full. Subscriptions for more than \$100,000 were allotted 29 percent but in no case less than \$100,000.

²⁰ Issued as a rollover of special bills maturing Jan. 16, 1957, and Feb. 15, 1957, respectively.

²¹ Subscriptions in excess of \$100,000 were allotted 31 percent for the certificates and 12 percent for the notes. Subscriptions for \$100,000 or less for both issues were allotted in full and subscriptions for more than \$100,000 were allotted not less than \$100,000. In addition to the amount allotted to the public, \$100,000,000 of the notes were allotted to Government investment accounts.

²² Redeemable at the option of the holder on Aug. 1, 1959, on 3 months' advance notice.

²³ In addition to the amounts issued in exchange, the Treasury allotted \$100,000,000 of each issue to Government investment accounts.

²⁴ Redeemable at the option of the holder on Feb. 15, 1960, on 3 months' advance notice.

²⁵ Subscriptions in excess of \$100,000 were allotted 22 percent for the certificates and 28 percent for the notes. Subscriptions for \$100,000 or less for both issues were allotted in full, and subscriptions for more than \$100,000 were allotted for not less than \$100,000. In addition to the amounts allotted to the public, \$100,000,000 of each issue were allotted to Government investment accounts.

²⁶ Subscriptions for \$50,000 or less were allotted in full. Subscriptions for more than \$50,000 were allotted 10 percent but in no case less than \$50,000. In addition to the amount allotted to the public, \$100,000,000 of the bonds were allotted to Government investment accounts. Payment for not more than 50 percent of the bonds allotted could be deferred until not later than Oct. 21, 1957.

²⁷ Subscriptions for \$10,000 or less were allotted in full. Subscriptions for more than \$10,000 were allotted 25 percent to savings-type investors and 12 percent to all other subscribers but in no case less than \$10,000. In addition to the amount allotted to the public, \$100,000,000 of the notes were allotted to Government investment accounts.

²⁸ Subscriptions for \$10,000 or less were allotted in full. Subscriptions for more than \$10,000 were allotted 26 percent to savings-type investors and 10 percent to all other subscribers but in no case less than \$10,000. In addition to the amount allotted to the public, \$100,000,000 of the bonds were allotted to Government investment accounts.

²⁹ Subscriptions for \$10,000 or less were allotted in full. Subscriptions for more than \$10,000 were allotted 20 percent but in no case less than \$10,000. In addition to the amount allotted to the public, \$100,000,000 of the bonds were allotted to Government investment accounts.

³⁰ Subscriptions for \$25,000 or less were allotted in full. Subscriptions for more than \$25,000 were allotted 24 percent but in no case less than \$25,000. In addition to the amount allotted to the public, \$100,000,000 of the notes were allotted to Government investment accounts.

³¹ Subscriptions for \$5,000 or less were allotted in full. Subscriptions for more than \$5,000 were allotted 60 percent to savings-type investors, 40 percent to commercial banks for their own account, and 25 percent to all other subscribers, but in no case less than \$5,000. In addition to the amount allotted to the public, \$100,000,000 of the bonds were allotted to Government investment accounts.

³² Subscriptions for \$100,000 or less were allotted in full. Subscriptions for more than \$100,000 were allotted 59 percent but in no case less than \$100,000.

³³ Subscriptions for \$100,000 or less for the bills and \$50,000 or less for the notes were allotted in full. Subscriptions for more than the minimum for each issue were allotted 44 percent on bills and 35 percent on notes but in no case less than the minimum. In addition to the amount allotted to the public, \$100,000,000 of the notes were allotted to Government investment accounts.

³⁴ Subscriptions for \$100,000 or less were allotted in full. Subscriptions for more than \$100,000 were allotted 47 percent but in no case less than \$100,000.

³⁵ Preliminary.

³⁶ Subscriptions from savings-type investors totaled \$720,000,000 and were allotted 70 percent. Subscriptions from commercial banks for their own account totaled \$470,000,000 and were allotted 35 percent. Subscriptions from all other investors totaled \$610,000,000 and were allotted 15 percent. Subscriptions for \$25,000 or less were allotted in full when accompanied by 100 percent payment at the time of entering the subscriptions. All other subscriptions for \$50,000 were allotted in full. Subscriptions for more than \$5,000 were allotted not less than \$5,000. In addition to the amount allotted to the public, \$50,000,000 of the bonds were allotted to Government investment accounts. Savings-type investors were given the privilege of paying for the bonds allotted to them in installments up to Apr. 23, 1959 (not less than 25 percent by Jan. 23, 1959, the issue date; 50 percent by Feb. 24, 1959; 75 percent by Mar. 23, 1959; and full payment by Apr. 23, 1959).

³⁷ Subscriptions for \$100,000 or less were allotted in full. Subscriptions for more than \$100,000 were allotted 60 percent but in no case less than \$100,000. In addition, \$100,000,000 of the notes were allotted to Government investment accounts.

³⁸ Subscriptions from savings-type investors totaled \$240,000,000 and were allotted 65 percent. Subscriptions from commercial banks for their own account totaled \$941,000,000 and were allotted 35 percent. Subscriptions from all other investors totaled \$322,000,000 and were allotted 20 percent. Subscriptions for \$25,000 or less from savings-type investors and commercial banks, and for \$10,000 or less from all other, were allotted in full. Subscriptions for more than these minimums were allotted not less than the minimums. In addition, \$50,000,000 of the bonds were allotted to Government investment accounts.

Source: Bureau of the Public Debt. Preliminary figures are from subscription and allotment reports; final figures are on "clearance" basis in daily Treasury statement.

PUBLIC DEBT OPERATIONS

TABLE 2.—Offerings of Treasury bills

[Dollar amounts in millions]

Issue date	Description of new issue							Amount maturing on issue date of new offering	Total unmat-ured issues out-standing after new issues
	Maturity date	Number of days to maturity	Amount of bids tendered	Amount of bids accepted					
				Total amount	On com-petitive basis	On non-com-petitive basis ¹	In ex-change		
Regular weekly bills:									
1959—									
Feb. 5	1959	91	\$2,299.9	\$1,399.7	\$1,134.2	\$265.6	\$219.9	\$1,802.0	21,006.3
May 7		182	716.1	399.9	371.7	28.2	20.7		3,600.7
Aug. 6		90	2,303.6	1,401.3	1,128.6	272.6	95.6	1,800.6	20,607.0
Feb. 13		181	725.3	400.0	373.6	26.4	21.4		4,000.7
Aug. 13		91	2,394.8	1,400.0	1,138.4	261.6	111.4	1,803.0	20,204.0
Feb. 19		182	922.1	401.1	372.6	28.5	6.1		4,401.9
Aug. 20		91	2,257.3	1,400.0	1,202.4	197.6	193.4	1,802.8	19,801.2
Feb. 26		182	754.6	395.4	370.0	25.3	3.9		4,797.2
Aug. 27		91	2,089.7	1,500.2	1,264.9	235.4	58.0	1,799.8	19,601.6
Mar. 5		182	724.2	400.1	375.3	24.9	14.5		5,197.4
Sept. 3		91	2,254.2	1,300.9	1,041.1	259.8	36.9	1,599.9	19,202.7
Mar. 12 ²		182	967.4	400.3	372.1	28.2	1.2		5,597.7
Sept. 10		91	2,019.4	1,300.6	1,023.8	276.8	40.6	1,600.4	18,902.8
Mar. 19		182	727.0	400.0	372.2	27.9	1.3		5,997.7
Sept. 17		91	2,122.4	1,300.1	1,041.1	259.0	75.2	1,600.8	18,602.2
Mar. 26		182	670.5	400.1	375.5	24.6	16.0		6,397.8
June 25		91	1,716.9	1,200.3	1,017.4	182.8	20.8	1,600.3	18,202.2
Apr. 2		182	796.7	400.1	383.9	16.2	.7		6,797.9
Oct. 1		91	2,074.1	1,200.1	989.0	211.1	151.9	1,599.3	17,802.9
Apr. 9 ³		182	765.1	400.0	377.6	22.5	20.9		7,197.9
Oct. 8		91	2,036.9	1,199.8	947.0	252.8	17.6	1,599.7	17,403.0
Apr. 16 ³		182	792.2	400.0	376.0	24.0	.9		7,597.9
Oct. 15		91	1,975.7	1,000.9	743.9	257.0	106.4	1,400.8	17,003.0
Apr. 23 ³		182	819.3	400.1	376.5	23.6	21.6		7,998.0
Oct. 22		91	1,926.9	1,002.0	761.6	240.4	102.9	1,399.3	16,603.8
Apr. 30 ³		182	862.7	400.2	378.9	21.4	20.7		8,398.2
Oct. 29		91	1,910.9	1,001.0	784.4	216.6	194.4	1,397.7	16,207.0
May 7 ³		182	760.5	400.0	383.3	16.8	43.6		8,798.3
Nov. 5		91	2,058.2	1,000.9	754.7	246.2	100.0	1,401.3	15,806.7
May 14 ³		182	867.5	400.2	376.2	24.0	26.2		9,198.5
Nov. 12		91	1,995.7	1,000.5	789.6	210.9	133.2	1,400.0	15,407.2
May 21 ³		182	832.0	400.2	378.3	21.9	20.7		9,598.6
Nov. 19		91	1,953.5	1,000.2	821.2	179.0	181.6	1,399.9	15,007.5
May 28 ³		181	858.6	400.0	381.3	18.6	22.6		9,998.6
Nov. 27		91							
Tax-anticipation bills:									
1958—									
Nov. 20		214	5,950.3	2,996.7	2,249.3	747.4			2,996.7
1959—									
Feb. 16		217	2,984.4	1,501.8	1,297.6	204.1			4,498.5
May 15 ³		221	1,699.2	1,499.8	1,389.9	109.9			5,998.3
Special bills:									
1958—									
Oct. 8 ⁴		219	5,804.6	2,735.4					2,735.4
1960									
1959—									
Apr. 1		289	3,444.9	2,006.2	1,733.3	272.9			4,741.6
May 11		340	3,463.9	2,003.3	1,703.4	299.9			6,744.9
								2,735.4	4,009.5

¹ For 13-week issues, tenders for \$200,000 or less from any 1 bidder are accepted in full at average price on accepted competitive bids; for other issues, the corresponding amount is stipulated in each offering announcement.

² Beginning Mar. 12, 1959, the 13-week bills represent additional issues of bills with an original maturity of 26 weeks.

³ Preliminary.

⁴ Issued on a fixed price basis; for details, see October 1958 bulletin, p. A-1.

⁵ May 15 maturity.

Source: Bureau of the Public Debt. Preliminary figures are from subscription and allotment reports; final figures are on "clearance" basis in daily Treasury statement.

The CHAIRMAN. The Senator from Connecticut is a very experienced dealer. I thought this was known to him, so I did not feel it necessary to elaborate originally, but I am very glad to affirm it now.

Senator BUSH. The Senator is wrong in that, too, because I am not an experienced securities dealer, and have not had any experience in dealing in securities for 25 or 30 years.

The CHAIRMAN. You are an underwriter, then.

Senator BUSH. No; I am not.

The CHAIRMAN. Well, some day we will converse as to precisely what it is.

Senator BUSH. There must be something wrong with me, but the Senator does not know what it is.

Secretary ANDERSON. Use of the advisory groups seems to me, Mr. Chairman, to be a useful technique in giving us the opportunity of assessing markets, determining the judgment of others as to whether or not a market exists for this kind of security or that kind of security, to get some idea of the relative size of those markets, and does not minimize the competitiveness with which the securities were bid. When the offering is announced, certainly anyone who wants to can buy it.

The CHAIRMAN. I will merely conclude with this observation, tying this matter up with the point raised by Congressman Coffin: Namely, that if you were to use the auction method and prepare the country for the issuance of a given interest rate and maturity, and then let people bid as to the price which they would pay, you would then have a competitive rate and it would not be necessary to go through this prior process of negotiation or collective bargaining which, if it were in the field of labor, would be denounced by the financial writers as being noncompetitive, but which possibly they may not denounce as being noncompetitive because it is in the field of finance.

Secretary ANDERSON. Senator Douglas, even if we were going to auction more of our securities—and as I have explained to the committee, if we think we can expand the auction we will certainly do so, but even so, before we auction different types of securities, we would want to make quite widespread inquiry into the marketplace, and this same group of people would still serve a very useful purpose in trying to determine the extent to which the market exists.

The very last thing that would concern me would be the matter of price since there is only a small difference possible. The primary thing is the existence of markets in the various areas.

The CHAIRMAN. Of course, if you would have your analysts and statisticians and other experts just as you have now, you would not be operating in the void.

Secretary ANDERSON. No, sir; but we would still be seeking judgments of people who are operating it all across the country.

Representative CURTIS. I would like to ask the Secretary the point-blank question: Is the Treasury in favor of a more competitive bond market?

Secretary ANDERSON. Yes. The more competitive we get the better we like it.

Representative CURTIS. I just wanted to be sure of that. Naturally, I think that is sort of like being for mothers, and I am glad to know the rest of the members are for that.

The CHAIRMAN. Very much so.

Representative CURTIS. I hope you speak for the party, too.

The CHAIRMAN. But we want action, not words.

Representative CURTIS. All right. That is the question I was going on to.

The issue, of course, is over what particular techniques might produce a more competitive market. I frequently find that these glib generalities sound good, but when we get into the details of what particular program might produce a more competitive market in this instance, we often find that one may be labeled as being for that purpose but it frequently does just the opposite. If we are going to reach an issue in this area, and I hope we do, because I think there is an issue, it should be over what the gentleman on this side said he believes will produce a more competitive market, and then over what questions our side might want to raise on actions which might possibly produce a more competitive market.

Secretary ANDERSON. I certainly would be grateful to the committee for any suggestions that will increase competitiveness. As far as I am concerned, I am perfectly willing to increase auctions if we could solve all the problems that are connected with them. The statement which I am going to submit as a result of the request of the chairman and Congressman Coffin sets out these problems. I do not say that they are unanswerable ones. I would hope that there is an answer to most of our problems.

But we do have to look at the realities of the situation and try to develop it, if it can be developed, in a more workable manner.

Representative CURTIS. I hope in the name of doing something desirable we do not make things worse.

The question I ended my previous interrogation with has been pretty well gone over here in different aspects, but I did want to ask two questions that somewhat bear on it, by making a statement first and then asking the question.

Many people want the Federal Reserve Board to engage in swapping operations as between long and short terms, but the Federal Reserve Board and Treasury have worked out, as near as I can figure, a kind of specialization in which the Federal Reserve Board concerns itself with money supply conditions, while the Treasury as an arm of the executive branch concerns itself with the level and structure of interest rates.

Thus, given the fact that substantial refundings of the Federal debt must be carried out each year, the Treasury can effectively carry out certain swapping operations. But the question is this: Can this swapping technique now be utilized by the Treasury?

Secretary ANDERSON. Is your question addressed to the advanced refunding?

Representative CURTIS. Yes.

Secretary ANDERSON. One of the elements of the proposals which we have made to the Congress, of course, is to allow the Secretary of the Treasury to provide for advance refundings, without taking the consequence of loss or gain at the particular time the exchange is made.

This is because, if we have this privilege—and for the most part it would be postponing a loss, rather than—

Representative CURTIS. If I may interrupt, that is part of the Treasury proposal in its debt management bill presently in the Ways and Means Committee.

Secretary ANDERSON. Yes.

Then, you see, some of the holders of long-term securities who would normally sell them as they grow short, would be persuaded to exchange in advance and keep invested in longer term bonds, which is what

they want. This would be one of the ways in which we would hope to secure a substantial amount of debt extension.

Representative CURTIS. The other question I had was proposed by the staff, and we feel it should be clarified.

What rationale lies behind the Treasury's interest in lengthening the average maturity of a debt during periods of economic expansion? In other words, what does it mean to say that issuing short-term debt is more inflationary than issuing long-term debt, as the Treasury has said on a number of occasions? Is there any comparable evidence to make this kind of statement?

Secretary ANDERSON. In the interest of time I would like to suggest that I submit a written statement on this subject.

Representative CURTIS. I wonder if he could submit a statement, Mr. Chairman, and then make a statement such as he would like now.

Secretary ANDERSON. If I am going to submit a written statement, I will defer oral statement now.

Representative CURTIS. I think it is a point that needs clarification. (The material referred to is as follows:)

As of mid-July the amount of Treasury marketable debt maturing within the next 12 months amounted to \$78 billion. In some ways, the volume of this short-term debt is as important a factor in our financing picture as the size of the total debt. Each time the Treasury goes to the market—either for refunding operations or for new cash borrowing needed to cover seasonal requirements or retirement of other securities—it is a significant event in all financial markets. Both the size of our borrowing requirements and the frequency of our trips to the market tend to interfere with the smooth marketing of new corporate and State and local government securities.

Another problem related to the large size of the debt maturing within 1 year is that such debt is only one step away from money. It should be realized, however, that in this country we have a large active and continuous demand for short-term debt instruments outside of the banking system inasmuch as corporations, State, and local governments, foreign accounts, and many other investors invest their short-term funds in this manner. Almost 60 percent of our under-1-year debt, therefore, is held outside of the banks—a larger percentage than in any other country we are aware of.

Nevertheless, heavy reliance in debt management on short-term issues is more inflationary than reliance on longer-term issues. The following points should be mentioned:

(1) Short-term issues are more suited to the investment requirements of commercial banks; consequently, there is a much greater chance that inflationary increases in the money supply will occur as banks create deposits to buy short-term Treasury issues. Conversely, longer term Treasury securities—particularly those with maturities of 10 years and longer—are more attractive to savings institutions, pension funds, and other institutions that invest a large portion of the savings of the public. To the extent that these institutions buy new Treasury issues, there is no growth in the money supply.

(2) Savings institutions and other investors that buy long-term bonds are seeking investments to hold in order to obtain a long-run interest return. On the other hand, many nonbank purchasers of short-term issues are simply investing temporarily idle funds; they intend to liquidate the securities later in order to spend for goods and services (e. g., business inventories, new plant and equipment), meet tax payments, or to take advantage of more favorable investment opportunities. They do this because the cost of shifting from a short-term issue to cash is likely to be much less than if they had purchased longer term securities, whose prices tend to fluctuate over wider ranges than short-term issues. This is what is meant by saying that "short-term securities are only a step away from being money." The holder can either sell the security in the market, or wait for it to mature within a few months or weeks, in order to obtain funds for spending. Consequently, there is much greater danger of a large shift from short-term securities to cash than from long-term securities to cash. Stated differently, the existence of a large vol-

ume of short-term Treasury debt reflects a high degree of liquidity in the economy; individuals and institutions are in a much better position to liquidate securities, obtain cash, and spend for goods and services—thereby augmenting inflationary pressures—than if more of the Treasury debt consisted of firmly held, long-term securities.

(3) When and if liquidation of short-term securities by temporary holders takes place, the inflationary impact of the shift is magnified to the extent that they sell the securities to commercial banks, inasmuch as bank purchases tend to increase the money supply. However, spending may expand rapidly even though banks do not purchase large amounts of the short-term securities liquidated by other market holders. As short-term interest rates rise, individuals and institutions with relatively large idle demand deposits in commercial banks may purchase the short-term issues. These deposit balances, previously idle, will be transferred, in effect, to individuals and institutions who use them for spending. This means that the velocity of money—or its turnover—tends to increase, thereby stimulating inflationary pressures in much the same way as an expansion in the money supply.

It should be noted that the large flotation of short-term Treasury issues during the past fiscal year has not as yet exerted strong inflationary pressures; these issues were largely taken up by business corporations which were experiencing rapid growth in liquidity as profits rose from recession lows. Moreover, we expect that corporate demand for short-term Government securities will remain active for several months to come, consistent with continued growth of corporate tax liabilities. However, as business activity continues to advance, a point is likely to be reached where corporations will be seeking funds to invest in inventories and plant and equipment. They may, at that time, tend to shift from net buyers to net sellers of short-term Treasury securities. The spending made possible by such sales would tend to add to pressures in the economy. Moreover, unless there is a current budget surplus, these securities would probably be sold to commercial banks and the money supply would expand, adding even further to inflationary pressures.

Even though it is preferable to have large amounts of short-term securities in the hands of nonbank investors rather than in commercial banks, we must never lose sight of the fact that a well-balanced debt structure calls for continued offerings of intermediate and longer term securities, whenever conditions permit, if debt management is to be conducted in a manner consistent with economic growth and stability.

The quest for a balanced structure of the debt is never ending since the passage of time brings more and more of the outstanding debt into the short-term area. The high point of our under-1-year debt was reached at the end of 1953 when the total was \$80 billion. The total is now \$78 billion, having dropped below \$60 billion for short periods in 1955 and 1956.

If the Treasury should be able to do nothing but issue under-1-year securities to replace maturing issues between now and December 1960, instead of the present \$78 billion, we would have almost \$100 billion of under-1-year debt outstanding at that time.

The Treasury does not intend this to happen. We must, therefore, continue to sell intermediate and longer term bonds whenever appropriate as we try to keep the short-term debt from growing. The only reason we have been able to keep the short-term debt from growing since December 1953 is that since then we have issued \$34 billion of 5-to-10-year bonds, \$2 billion of 10-to-20-year bonds, and \$6½ billion of over 20-year bonds.

Representative PATMAN. Mr. Secretary, did you say you would furnish this information I requested at the beginning of my interrogation before?

Secretary ANDERSON. Congressman Patman, I will be glad to furnish it by the classifications which we have. I would not want to give names of individual holders, but by given classes of individuals I will be glad to furnish it.

Representative PATMAN. But you will break it down into categories, so it will be meaningful?

Secretary ANDERSON. Yes, as nearly as we can.

Representative PATMAN. The information I gave about the \$681 million profits last year of member banks—the securities transactions can be obtained from page 654 of the June Federal Reserve Bulletin. It is broken down as to groups of banks, sister groups.

Then, on page 659, you will find information for particular years, like 1958, which was \$681,554,000 profits on securities. The preceding year was \$64,368,000, and the year before that, 1956, was \$31 million. So it was more than 20 times as much as it was in 1956, and I say that is enough to excite inquiry and suspicion.

Representative CURRIS. The reason I wanted the source was that I wanted to be able to evaluate the information.

Incidentally, I would appreciate a statement from the Treasury on their analysis of this, because I think it is a very important point.

Secretary ANDERSON. Senator Javits asked for both profit and loss.

Representative PATMAN. I desire to call the Secretary's attention to the fact that the high interest policy which has been pursued for the last 6 years has had a devastating effect on the farmer, for instance. During the year 1952, the farmers' income was \$15.3 billion. It has been reduced every year since then. Until now, as of June 1959, it was down on the basis of \$12.1 billion, which is about \$3.2 billion.

On the money lenders' income, or personal interest income, it was \$12.1 billion in 1952, but it increased greatly in 1953, to \$13.4 billion. It has increased every year since that time, and in June 1958 it was on a basis of \$20,400 million as compared to \$12,100 million at the beginning of 1953. This year, in June 1959, a year later from the time it was 20 billion 4, it is now 22 billion 2, as disclosed by the economic indicators for July on page 4.

So you realize, do you not, Mr. Secretary, that high interest is taking too much of our national income?

Secretary ANDERSON. Congressman Patman, I would find it very difficult to single out any single factor and say that this is the factor which determines the rise or fall of farm income. This has to be weighed in the light of the whole complex problem of the farm situation as it has existed over these years.

Also in determining the relative cost of income increase, one must take into account the fact that we have increased the total national debt. As we increase the total national debt, of course, we have more debt to service.

Also paid as a part of this personal income interest is the income which is paid on the savings bonds and that sort of thing, which 40 million Americans hold. So there is quite a widespread ownership of the interest. It is not all concentrated.

One has to weigh these things in the context of the complexity of our country and the ownership of the debt in order to come out with a fair figure.

Representative PATMAN. About the E-bond figure which you are asking to increase, you are asking to increase it to about 3¾ percent; are you not?

Secretary ANDERSON. Yes.

Representative PATMAN. Will you not be in the same unfavorable situation, then, as you are now, because many of the savings and loan associations are offering 4.5 percent, guaranteed by the Government,

and you cannot say that that would relieve the situation, because it would still be three-quarters of a percent under what they could get guaranteed by the Government? Would you not still be in the same unfavorable position, if you had $3\frac{3}{4}$ percent?

Secretary ANDERSON. I do not believe, as far as I know, a large proportion of the savings institutions have gone quite that high.

Representative PATMAN. A large proportion have gone over it.

Secretary ANDERSON. Quite a few have gone to 4 percent, yes.

Representative PATMAN. And you would still have the same unfavorable situation, Mr. Secretary.

Secretary ANDERSON. At the same time, historically we have been falling behind since the war. The earning position of other types of savings has improved faster than ours. The thing, of course, that has helped us is the fact that we have the largest volunteer organization in the world trying to help us sell these securities.

Representative PATMAN. But do you have any evidence to support the statement that a higher interest rate would cause more savings?

Secretary ANDERSON. You mean generally over the country?

Representative PATMAN. Yes. In the past I think the evidence would disclose that it has not affected savings at all, that savings have been just as much and more when interest rates were low as they were when they were high.

Secretary ANDERSON. It would affect the sale of the securities. When you get into periods of recession, the whole group of prices goes down.

Representative PATMAN. You are talking about E-bonds now.

Secretary ANDERSON. Yes, but the amount of savings in E-bonds went up last year. We gained, as I recall, about \$1 billion last year, and our higher rate of interest helped. But now our cash-ins are increasing, and our sales are declining.

Again, I have said if one looks at the trend in individual savings in the past several years in this statement which I gave to the House committee, savings and interest rates in savings and loan associations have both gone up sharply, mutual savings banks up sharply, commercial bank savings up sharply, and the E-bonds not nearly so sharply.

But what we are trying to do here now is to at least get into a position where we can maintain equilibrium with the cash-ins and maturities of the older series we are paying off now.

Representative PATMAN. Mr. Secretary, should we ever give a sufficient interest rate to attract savings to the extent that they would want to keep their money in savings accounts rather than looking for some desirable investment to put their money in?

Secretary ANDERSON. You would want to be fair with your customers. As I have indicated, we would not have the belief that we ought to siphon off all the savings in the country into Government securities. We know that if we are to grow and prosper in our country, there has to be investment of all kinds. But as to the extent to which people want to save and accumulate, we must treat them fairly both as to their earnings and as to the protection of their purchasing power.

Representative PATMAN. Mr. Chairman, I have a number of questions but I shall not insist on them if you do not want to have a hearing this afternoon. And Mr. Coffin has a question he wants to

ask. If other members do not want to come back this afternoon and the Secretary will agree to answer these questions in written form for the record, it will suffice in my case.

Secretary ANDERSON. I will be delighted to.

(The questions which Representative Patman asked the Treasury to answer follow:)

The Treasury has expressed its willingness to answer each of these questions as fully as is necessary, but present heavy burdens on the small Treasury staff precludes an early response. The Treasury will make every effort, however, to transmit the replies to these questions as expeditiously as possible. (See Part 6C of the hearings.)

QUESTIONS FOR SECRETARY ANDERSON (PATMAN)

1. With reference to your request for repeal of the interest rate ceiling on Treasury bonds, how high will long-term rates go if the ceiling is taken off?

1a. The Federal Reserve could, if it wished to do so, drive the rate on long-term Governments to 6 percent, could it not?

1b. What assurance do you have that the Federal Reserve will not drive the rate to 6 percent, or even to 7 percent?

2. Why have interest rates gone so high? What are the most important causes?

3. What is the reason for the flight of money from bonds to stocks?

4. Do you have any evidence that people have saved any larger percentage of their incomes when interest rates were high than when interest rates were low?

5. What is your understanding of what the main problem is at the present time that the Fed is trying to solve by its present money policy?

6. Is it your understanding that the main impact of monetary policy is through interest rates or through the amount of credit available?

7. How much has the cost of living increased in the last 18 months?

8. And what is the present interest rate on 91-day Treasury bills?

9. (Omitted.)

10. Is the difference accounted for by a greater demand for savings?

11. Is it accounted for by investors' expectations of inflation?

12. Do you think that the administration's massive verbal attack on inflation, its constant warnings that inflation is coming, could be the whole cause of the need to remove the interest rate ceiling?

13. Do you think that investors' fear of inflation is substantially justified by the facts?

14. Many of the newspapers and magazines have been carrying ads placed by the insurance companies and others which say "Help Fight Inflation," or "Inflation Shoots Holes in Everybody's Pocketbook," and so on. Do you know whether or not the cost of this advertising is tax deductible as a business cost of these corporations?

15. Why is it the Treasury thinks that the debt should be lengthened?

16. Is it the Treasury's policy to manage the debt in ways to help out in economic stabilization, or is it the policy to try to obtain the lowest interest cost without respect to economic stabilization?

17. What criteria does the Treasury use for determining when to issue long-term debt and when to issue short-term debt?

18. Why didn't the Treasury pay off its short-term debt and issue long-term bonds last year, particularly in the first half of last year, when long-term rates were low?

18a. Does the Treasury have in mind an approximate amount of debt which would be shifted from short term to long term if the interest rate ceiling is repealed? If so, can you give us an indication of what you think it is?

18b. Assuming that by next year or the year after we may have a low interest rate policy again, what are the relative advantages and disadvantages of the Treasury's confining itself to short-term issues in the meantime, even though the short-term rate goes to, say, 5½ percent?

19. With reference to the long-term issues of the last several years, is it true that almost all of these have immediately gone to a premium after they were issued?

20. Does the fact that an issue is immediately reselling at a premium indicate that the interest rate the Treasury put on the issue was too high?

21. When an issue is oversubscribed by 4 to 1, doesn't this indicate that the interest rate put on the issue is a great deal higher than it needs to be?

22. Do I understand right, that an insurance company, let us say, that wants to buy \$1 million worth of an issue will subscribe \$4 million worth if it thinks the issue will be oversubscribed by 4 to 1?

23. What happens when a man's allotment is a great deal more than he expected you to give him? Is he forced to take the whole amount?

24. A man who receives an allotment of an issue much bigger than he expected to get, could be embarrassed financially, could he not, and actually suffer a loss?

25. Have you had many instances recently where people were financially embarrassed by receiving an allotment larger than they could handle?

26. How do you account for the fact that so many investors think they can guess in advance what the total offer will be on a particular issue?

27. Secretary Humphrey is reported to have said that the Treasury has no control over interest rates, that it simply goes to the market, like going to the market for a dozen eggs. Do you agree that the Treasury is that helpless over that interest rate it must pay?

28. In 1958, total security issues of the Federal Government, the State and local governments, and the corporations came to \$81.4 billion. Of that amount \$62 billion was in issues of the Federal Government, not counting Treasury bills. Wouldn't you agree that since the Treasury controls such a large percentage of the total supply of issues—\$62 billion out of \$81 billion—it necessarily has a great deal of discretion as to the rates it can set?

29. With reference to the Treasury's advisory committees, how do these committees go about determining how much interest there will be in an issue? Do they poll the investors in their fields, and, if so, do you know what percentage of the market they poll?

30. Has the fact that so many large investors and dealers all think they can guess what the total offer will be on an issue, and are willing to back up their guess with a financial commitment on which they could lose their shirts, suggested to you that some of the elements of competition may be missing in the market for Government securities?

31. If I may I would like to read you a brief paragraph and then ask you to comment upon it:

"Among the more important interest rates, one group in which price leadership and price administration play decisive roles is the rate structure charged by commercial banks for industrial, agricultural, and commercial loans. New departures in this rate structure are ordinarily signaled by one (not always the same) major bank, in a manner quite similar to price leadership in steel or aluminum. The last important signal, given on May 15, called for an increase from 4 percent to 4½ percent on prime risks and corresponding adjustment of other rates. There was little criticism of the commercial banks for raising their prices by 12½ percent at one swoop. Was this not an inflationary action? The banks made just as many loans at 4½ percent as they would have at 4 percent and to the same people. The price had merely gone up. What would have been said about any group of wage earners who raised the price of their services by 12½ percent in one step?

"In its general interest structure, the ordinary commercial bank follows national and regional price leadership. The individual loan operations of a commercial bank also bear only a remote relationship to our traditional picture of competitive practice—and necessarily so. A bank does not auction credit to its customers; it rations credit among them. The total amount the banking system has for rationing among its customers is determined not by any action of private bankers but by the reserves supplied by the Reserve System * * *"

Would you agree that that is a fairly accurate description of how commercial bank interest rates are determined?

32. Has it been your observation that after the banks are given excess reserves, the banks don't always reduce their lending rate, and at other times several weeks go by before bank rates are reduced?

33. With reference to the Treasury's advisory committees, since you have been Secretary have these different committees given any substantially different advice as to what the interest rates should be on any particular issue being contemplated? Have the interest rates recommended by the various groups differed by more than one-eighth of a percentage point?

34. Since you have been Secretary, has the Treasury fixed a rate on an issue which was different from the rate recommended by the Treasury's advisory committees?

35. If so, can you recall what rates were recommended and what rates you actually put on the issue? (Supply exact information for the record.)

36. As to the terms of the securities issued since you became Secretary, has the Treasury gone substantially against what the advisory committees recommended?

37. Have the different advisory committees given substantially different recommendations as to what the term of an issue should be?

38. Has the Treasury felt any dissatisfaction with the auction method by which Treasury bills are sold? Do you have in mind any significant improvements that might be made in the auction technique?

39. With reference to the Fed's open market operations, you know about the 17 dealers with whom the Open Market Committee does all of its trading? Is it your understanding that the Open Market Committee gives those dealers support at times—in other words, when the dealers are overloaded with bills, the Open Market Committee bails them out either with loans, which they call repurchase agreements, or by buying in some of their bills?

40. Why doesn't the Treasury sell all of its marketable securities by the auction method?

41. Isn't the auction method the best method for finding out what the lowest rate is the Treasury has to offer in order to sell a given quantity of securities? In other words, the auction method seems to do away with guessing what the market rate is and avoids the risk of guessing too high?

43. Has the Treasury ever tried to sell a long-term issue by the competitive bid method?

44. Has the Treasury made any factual studies to determine whether it gets a wider distribution of its securities among initial purchasers by the fixed-price method than it would get by the auction method?

45. When an issue is oversubscribed, what is the Treasury's method of determining the allotments?

46. In view of the statement frequently made that the Treasury wishes to get its securities into the hands of savers, why is it that it allots a portion of oversubscribed issues to the commercial banks?

47. Has the Treasury given serious consideration to a policy not to allot any portion of an issue to commercial banks when the full issue can be sold to savings-type investors?

48. Does the Treasury plan, in the period ahead, to make fewer offerings in larger amounts or to make more or less regular offerings in smaller amounts?

49. Has the Treasury considered the question whether the Federal Reserve should be directed to buy all new Treasury issues and thus assume an underwriting function?

(a) If "Yes," what are the disadvantages?

50. Would you agree that if the Federal Reserve did buy all new issues directly from the Treasury and raise reserve requirements of the member banks temporarily to offset the credit increase, the Fed would then be in a good bargaining position to sell the securities at a low interest yield, because the banks would understand that the Fed would reduce reserve requirements only as and if they bought the Government securities?

51. Has the Treasury considered the advantages of setting up a stabilization fund to help in stabilizing the market for its new issues?

52. Has the Treasury considered the advantages and disadvantages of carrying a larger cash balance?

(a) If "Yes," would the fact that the Treasury could defer financing, when the times are not propitious, more than offset the cost of carrying the larger balance?

(b) Is there anything to be gained from carrying a larger cash balance by reason of the fact that the Treasury would be in a position to defer financing when it thinks market expectations as to interest rates are unrealistic?

53. With reference to the 4.7 percent interest yields at which the Treasury sold bills week before last, and the 4¾ percent rate on short-term issues announced last week, do you feel that these rates were too high?

(a) What about your authority to sell up to \$5 billion of obligations directly to the Federal Reserve? Why was that not used?

(b) What changes are needed to make your authority to sell securities directly to the Federal Reserve more effective?

54. Has any consideration been given to the question whether the Treasury should have more discretionary authority in managing the Government trust accounts?

55. Would the Treasury do better to turn the marketing of its securities over to private underwriting syndicates, such as market corporate securities?

TREASURY BANK DEPOSITS

56. What was the Treasury's average deposit balance with the commercial banks last year?

(a) What is the average balance so far this year?

(b) Can the Treasury disburse funds on deposit with the private banks directly from those banks, or must it first call the funds in to a Federal Reserve bank?

(c) What would be the disadvantage of the Treasury's promptly calling its funds into the Federal Reserve banks and having the Federal Reserve banks invest these funds in short-term securities?

(d) What would be the disadvantage of permitting the private banks to pay the Treasury interest on its deposits?

57. The depression-time bank crisis is long since past, yet the law prohibiting commercial banks from paying interest on demand deposits is still on the books. Would you agree that this law is now obsolete and that it should be repealed?

MONETARY POLICY

1. Do you think it would be wrong or against the public interest for Congress to express disagreement with the Fed's monetary policies, if it does disagree?

2. Would you think it wrong or not in the public interest for the Treasury to express disagreement with the Fed's monetary policy, if it does disagree?

(a) If "No," are you in complete agreement with the Fed's monetary policy at the present time?

(b) What changes in monetary policy would you suggest?

(c) Without reference to whether the same degree of credit restraint should be maintained, do you know of any changes in the Fed's method of operations that would improve the Treasury's debt management problems?

3. When the Fed decides to increase the amount of credit in the banking system by a given amount, is it more inflationary for the Fed to bring about the increase by buying Government securities in the open market, or by reducing required reserves of the member banks? Why?

(a) What are the relative advantages of the two methods from the standpoint of the Treasury?

(b) What are the relative advantages from the standpoint of monetary controls, as you understand them?

(c) Did the Federal Reserve obtain the Treasury's advice on whether it should acquire part or all of these securities, or whether the Fed should make it possible for the member banks to acquire them?

4. In the first half of 1958, the Fed reduced required reserves of the member banks by \$1.5 billion, which was enough to allow these banks to increase their loans and investments by \$10.5 billion. The member banks used this power to create new money to acquire \$10.4 billion of Federal securities. Would the Treasury's problem be substantially different today if the Fed had itself acquired that \$10.4 billion of Federal obligations?

(a) What would the difference be?

(b) Which method of increasing the money supply is more likely to reduce interest rates on Government securities?

(c) If "Yes," what advice was given?

(d) Do you regularly obtain advice from the Fed as to the terms and interest rates you should set on the bonds you issue?

5. It is sometimes said that member banks' reserves are funds which the banks have deposited with the Federal Reserve banks, and that the member banks are thus denied the opportunity to use their own money. What is your understanding as to the sources of member bank reserves?

6. If member bank reserves have been created by the Fed itself, and by the Treasury, and the member banks have been allowed to create several dollars of money for each dollar of reserves, do you see where there is any burden being imposed on the member banks by requiring them to keep these reserves on deposit?

7. With reference to the amendment which has been placed on the bill to remove the interest rate ceiling, I believe you first testified that you could live with this amendment. What is your present position on the amendment?

(a) What has caused you to modify your views on the amendment, if they have been modified?

"BILLS ONLY" POLICY

8. With reference to lengthening the maturity of the debt, should there be some authority for the Treasury to swap securities with the Federal Reserve—say, to swap long-term issues for short-term issues being held in the Fed's portfolio?

9. What has been the effect of the "bills only" policy on debt management—has it made the problem easier or harder?

10. What has been the effect of the "bills only" policy on the relationships between short-term, intermediate, and long-term interest rates?

11. It is my understanding that at times the purpose of the Fed's tight-money policy has been mainly to dampen an investment boom. What interest rates most affect the level of investment the short-term or the long-term?

12. Has the Treasury found that high interest rates have, in fact, caused the big corporations to postpone or to cancel their expansion plans to any substantial extent?

GOLD OUTFLOW

13. With reference to gold, the International Foreign Trade Council predicted this week that this country will have a deficit of about \$5 billion in its international balance of payments this year. That would probably mean a \$5 billion loss in the Treasury's gold stock, would it not?

(a) Do you agree with the proposition that interest rates should be high in order to hold funds in this country?

(b) Do you agree with the proposition that further wage increases pose a serious threat to our gold hoard, because we may be priced out of foreign markets?

(c) How much of the expected deficit in the international balance of payments this year will result from an adverse balance of trade—that is, from trade in actual goods and services?

(d) How much of the deficit is expected to result from a net export of capital, and how does this amount break down as between foreign aid and other capital movements?

(e) How much U.S. money is going abroad to speculate in foreign stock markets?

(f) Do you think it desirable to curb U.S. speculation or investment in foreign stocks?

(g) Do you think that the threat to the Treasury's gold stock is serious enough that we should cut back on foreign aid?

Representative PATMAN. If you want to come back, I will be glad to cooperate, Mr. Chairman.

Secretary ANDERSON. I will be glad to answer any question from any member on that basis.

The CHAIRMAN. Congressman Coffin.

Representative COFFIN. Mr. Chairman, I just want to ask one question, following up on your series of questions of the Secretary with regard to the advisory committees that are called in when prospective issues are contemplated.

It just seems to me that facing the tremendous marketing problems which we do, it is worth exploring whether or not the Treasury could conduct market analyses, professional spot or comprehensive market analyses, as an automobile manufacturer does when he contemplates a new model, or as any large organization does. In other words, here you are with perhaps the biggest sales job of any executive in the country. You have your internal staff constantly making studies, I know. Then you check it with the advice of the committees, who are also skilled. But it seems to me that you should professionalize this, systematize this, to the extent that you have people in this field making this kind of market analysis. This is not unique. This is done in other areas.

Secretary ANDERSON. Congressman, we do it to the extent that we can. Under Secretary Baird makes swings around the country at

various times for this specific purpose. Mr. Mayo makes other swings around the country. We try to talk to all kinds of investors, people who are handling pension trust funds for States and that sort of thing.

Representative COFFIN. What I have in mind is, when you foresee particular issues, that you have a force in the field, either on contract or permanent staffs, inquiring as to alternatives to particular issues, in order to get a résumé on a systematic basis as to what the temper might be.

Secretary ANDERSON. I think this is a technique worth studying. Also one would say that you have the choice: Do we send out technicians to talk to 40 members of a certain kind of banking institution, or do we ask 40 members of the banking institution to come in and say, "This is what we think about the markets"?

Representative COFFIN. You know, in a court trial, if it is very, very important that one witness not be influenced by another, you examine him in the absence of the other witness. I would think that there would be something to say for the individual approach, although it might not be as convenient.

Secretary ANDERSON. We do that also, sir, with even the members of the advisory committees.

The CHAIRMAN. I think this has been a very interesting morning. There are certain questions which I should like to read, and which I hope the Treasury can respond to, because we know you are very busy, and it would be an imposition to ask you to come back this afternoon.

The Treasury maintains rather large deposits in the banks of the country. People who have as diverse fiscal ideas as Senator Byrd and Congressman Patman and myself, have from time to time urged that on some of these deposits the Government should get interest instead of their being free as now.

I should like to address these questions to you.

1. Why should not the Treasury require the banks to pay interest on the minimum balance maintained by the Treasury with the banks or convert some of these deposits into time deposits on which it would draw interest?

2. If the commercial banks are not to pay interest on Treasury accounts, why should not these funds be drawn properly back into the Federal Reserve, which could invest them in short-time Treasury bills until the Treasury drew upon the Federal Reserve?

In this way, the Federal Reserve would be making earnings, and 90 percent of those net earnings would go back to the Treasury.

3. If the deposits are to be maintained in commercial banks, could not the Treasury work with a smaller balance and handle temporary surges or shifts in cash position by an increased use of its authority to draw temporarily on the Federal Reserve banks?

4. Would you agree that the law is now obsolete and should be repealed which prohibits commercial banks from paying interest on demand deposits?

I think those are extremely important questions. If you wish to answer them now, fine.

Secretary ANDERSON. I would be glad to answer them in detail in writing.

(The answers referred to are as follows:)

Question 1.—Why should not the Treasury require the banks to pay interest on the minimum balance maintained by the Treasury with the banks or convert some of these deposits into time deposits on which it would draw interest?

This is a question which can be answered only after a full discussion and understanding of how Treasury deposits with the banks are handled. The major portion of the cash held by the Treasury to meet its operating requirements is maintained on deposit in tax and loan accounts in 11,000 commercial banks throughout the United States. The balances with individual banks fluctuate widely from time to time and from bank to bank. They range from amounts of less than \$5,000 in the case of some of the smaller banks to amounts of several hundred million dollars on occasion in the case of the larger size banks in the country.

The balances which the Federal Government carries with commercial banks in the form of tax and loan accounts arise from the periodic payments of taxes and the proceeds of Treasury borrowing.

It should be borne in mind that the Treasury does not take the initiative in depositing funds to tax and loan accounts, except in certain cases. Under conditions when net receipts in the Treasury's account at the Federal Reserve banks accumulate appreciably faster than had been estimated, excess funds may be deposited for a few days with class C banks (banks with total deposits of more than \$500 million) and then withdrawn, without notice, as soon as a more normal flow of funds is restored. Conversely, if the Treasury balance in Federal Reserve is below expectations, the Treasury often makes special calls on these same class C banks, without notice. The Treasury does not discriminate either among individual banks within a class or among the three classes in its conduct of these deposit or withdrawal activities. All withdrawals are based on a percentage of deposit balances in each bank as of a given date, and the same is true on any deposits made in class C banks.

The balances the banks acquire as the result of tax collections may arise in either of two ways. They may arise from soliciting their customers to deposit certain excise and withheld income and social security taxes with the bank instead of paying them to the District Director of Internal Revenue, which has the effect of giving the Treasury the immediate call on those funds rather than having checks outstanding for several days while the District Director processes them and deposits them at a Federal Reserve bank. In addition, balances arise from income tax payments which are credited directly during major tax payment periods to tax and loan accounts by the bank on which the taxpayer's check is drawn. In neither case does this represent an increase in deposits to the banks, but merely a transfer of balances on a bank's books from the account of the taxpayer to the Treasury's account.

The immediate transfer of these balances to the Treasury's account with the Federal Reserve banks would be a very disruptive influence to the money market and the whole economy. The tax and loan accounts, therefore, represent a mechanism helpful to the whole economy, not just to the banking system alone.

Furthermore, the law requires that banks pledge collateral, usually U.S. Government securities, to secure all funds in Government tax and loan accounts, which is a special condition that attaches only to public deposits. A bank has to have on hand at all times free collateral to cover the maximum balance it may hold in the tax and loan account, or otherwise it cannot accept the deposit.

These tax and loan balances must be subject to withdrawal on demand by the Treasury because they are the funds which are used from day to day to meet the expenses of the Government, and they fluctuate widely. It would not be practicable for the Treasury to shift any part of these balances into time deposits for the purpose of having them draw interest. Any surplus funds the Treasury might have in demand deposits would be more appropriately used to reduce the debt instead of converting them into time deposits.

These fluctuations are well illustrated by the fact that total balances on May 31, 1958, amounted to \$4¼ billion, and increased to to \$8¼ billion as of June 30, 1958; but by July 31, 1958, they had been drawn down to \$3¼ billion. Balances during the calendar year 1958 averaged less than \$3¾ billion, with balances running under \$1½ billion on several occasions. It should also be remembered that these balances typically include funds on which the Treasury has already given the bank notice of withdrawal to be effective in a few days, so the "free", or uncalled, balances which banks can actually employ are frequently quite low. In January 1958, for example, balances less outstanding calls were less than \$350 million on several occasions. Despite their wide fluctuations Treasury deposit balance are, of course, valuable to each bank in the same way as any other deposit. If a bank is to keep a deposit rather than lose it to another bank

it must accept the responsibilities which deposit maintenance and growth require. Prompt and efficient servicing of customers, whether public or private, is always important. Banks recognize that their Treasury tax and loan deposit carries with it important public responsibilities—including many services which the banks perform for the Government without specific charge.

A full discussion of the Treasury tax and loan account operations is contained in the Monthly Review of the Federal Reserve Bank of New York for April 1958. A copy is attached to the end of the reply to question 1.

The broadest aspect of this operation is that commercial banks have a special relationship to the U.S. Treasury in that their demand deposits provide almost 80 percent of the Nation's money supply as commonly defined, the balance being currency in circulation. Since they are so charged with acting in the public interest they are carefully regulated by Federal and State supervisory authorities as to almost every phase of individual bank practices, as well as being subject to the powerful effects of the actions of Federal Reserve monetary policy on the banking system as a whole. They are not free agents, and on many occasions their ability to expand their volume of profitable loans as much as they could otherwise expect to do has to be curtailed severely by the requirements of national economic policy.

In addition to the monetary function performed by the commercial banking system, the banks operate as a direct arm of the Treasury in other ways. The banking system is a focal point in the efficient public distribution of upward of \$50 billion a year of Treasury marketable tax anticipation bills, 1-year bills, certificates, notes, and bonds, plus \$1½ billion or more regular weekly bills on the average.

The Treasury, unlike corporate or State and local government borrowers, has no underwriters for its securities in the usual sense of that term. In other words, the Treasury pays no commissions to the banks that help place Treasury securities with their ultimate holders. The Treasury, therefore, depends heavily upon the commercial banking system to solicit orders for huge issues of Government securities on which the books are open only from 1 to 3 days. An overwhelming share of all subscriptions for new issues of Government securities are handled by the commercial banks. Without their active solicitation and processing of these subscriptions, the Treasury operations on the scale now conducted would be much more difficult as well as expensive.

In addition, banks actively help the Treasury promote the sale of U.S. savings bonds, sometimes at the expense of their own savings deposits. They do this not only through their own functions as issuing agents in over-the-counter sales and as managers of their own payroll savings plans, but also in their communities by helping to acquaint an increasing number of citizens with the advantages of savings bonds and in assisting business concerns in setting up and maintaining active payroll savings plans.

The suggestion has been made from time to time that perhaps the Treasury would be better off if banks were required to pay interest to the Treasury on tax and loan account balances and that, in turn, the banks should charge the Treasury for the services it performs. Many of these services are not susceptible to precise cost measurements, so the designing of a comprehensive system of fees necessary to completely reimburse commercial banks for their services to the Treasury would be extremely complicated. Furthermore, it would reimburse banks for what are now free services, which services are also performed without charge by other entities. If the banks were to charge the Treasury for all savings bonds that they sell, for example, those corporations throughout the country which in the aggregate issue millions of series E bonds each year and keep extensive records of payroll deductions would certainly ask the Treasury for reimbursement for their services. Similarly, all business concerns in the country would be encouraged to ask the Government to defray their costs of withholding income taxes and social security taxes from employees pay checks if the banks were reimbursed for handling the deposits represented by those taxes.

The impact of a uniform fee system would fall unequally on different banks, favoring the larger more highly mechanized units. Yet a fee system which attempted to take cost differentials into account would open a new area of controversy. Furthermore, the fee system in terms of cost of clerical help presumably would have to be reviewed from time to time as conditions change.

Problems arising from the suggestion that interest be paid on demand deposits generally are discussed in the reply to question 4. It should be mentioned here, however, that it would be unfair for the Government to require by law that

banks pay interest on the demand deposits of the Government which because of their rapid turnover are less desirable than many other types of deposits, while at the same time the law prevents banks from paying interest on demand deposits to State and local governments, to business firms, and to individuals.

Total demand deposits (other than interbank deposits) as of December 31, 1958, for example, amounted to \$134.3 billion, of which \$4.2 billion, or only 3 percent, was accounted for by demand deposits of the U.S. Government. State and political subdivisions alone had \$10.9 billion of demand deposits on that same date, or $2\frac{1}{2}$ times the Federal total, despite the fact that U.S. Government operations are far larger.

The Treasury makes it a policy to keep its working balances adequate but never excessive. Including deposits in Federal Reserve banks (usually about \$500 million) and gold in the Treasury general fund (formerly as high as \$1 billion, but currently only about \$100 million, the Treasury's cash balance has averaged about \$4 $\frac{1}{2}$ billion during each of the last fiscal years. This is relatively small; the average operating cash balance this year has averaged only 69 percent of average monthly budget expenditures—the lowest percentage for any recent year. The Treasury's cash balance is no higher today than it was a decade ago, when budget spending was half its present rate.

The efficient use of cash balances in this way has, however, gone about as far as it can without impairing efficiency of Treasury operations. There are times when a somewhat larger cash balance would have given the Treasury much needed flexibility in timing its borrowing operations so that it could ride out a period of market apathy for new issues, rather than forcing the Treasury to borrow in an unfavorable atmosphere because it was running out of cash.

But an adequate appraisal of the value of bank services in itself presents difficult problems. Despite these difficulties, however, the Treasury is undertaking a careful study of costs which banks incur in performing functions for the Treasury in those situations where costs are subject to specific measurement (see attached letter) although we do not expect that the resulting partial data will offer any indication as to the true burden of bank operations on behalf of the Treasury.

THE SECRETARY OF THE TREASURY,
Washington, June 12, 1959.

HON. JOSEPH CAMPBELL,
Comptroller General of the United States,
Washington, D.C.

DEAR MR. COMPTROLLER GENERAL: I have your letter of June 3 concerning our recent discussion relative to your suggestion that the Treasury make a study to determine whether or not balances in tax and loan accounts may have produced income to the banks in excess of the cost of the services performed by them for the Federal Government and for which they are not otherwise compensated.

As we have tried to make clear in conversations with you, we believe there are overriding considerations of monetary and debt management policy that cannot be resolved by a study of the character indicated. However, in view of your conviction that the Treasury should make such a study, we will undertake one as promptly as possible. As I pointed out in our discussion, the Treasury has an exceptionally heavy load of financing to do in the next 3 months, and in addition we have a heavy legislative program now pending in Congress relating to public debt management.

We hope to have the study initiated within 90 days, and I shall notify you when it is undertaken.

Sincerely yours,

(Signed) ROBERT B. ANDERSON,
Secretary of the Treasury.

[Monthly Review, April 1958—Federal Reserve Bank of New York]

THE TREASURY'S DEPOSIT BALANCES AND THE BANKING SYSTEM

Financing the Federal Government's operations involves huge and irregular transfers of funds between the Treasury and the general public. While some progress has been made in recent years in reducing the extreme fluctuations in the Treasury's receipts and payments, the remaining swings still are sizable. Moreover, they are likely to continue to be large, because of the vast scale of the Government's financial operations and the unavoidable concentration of

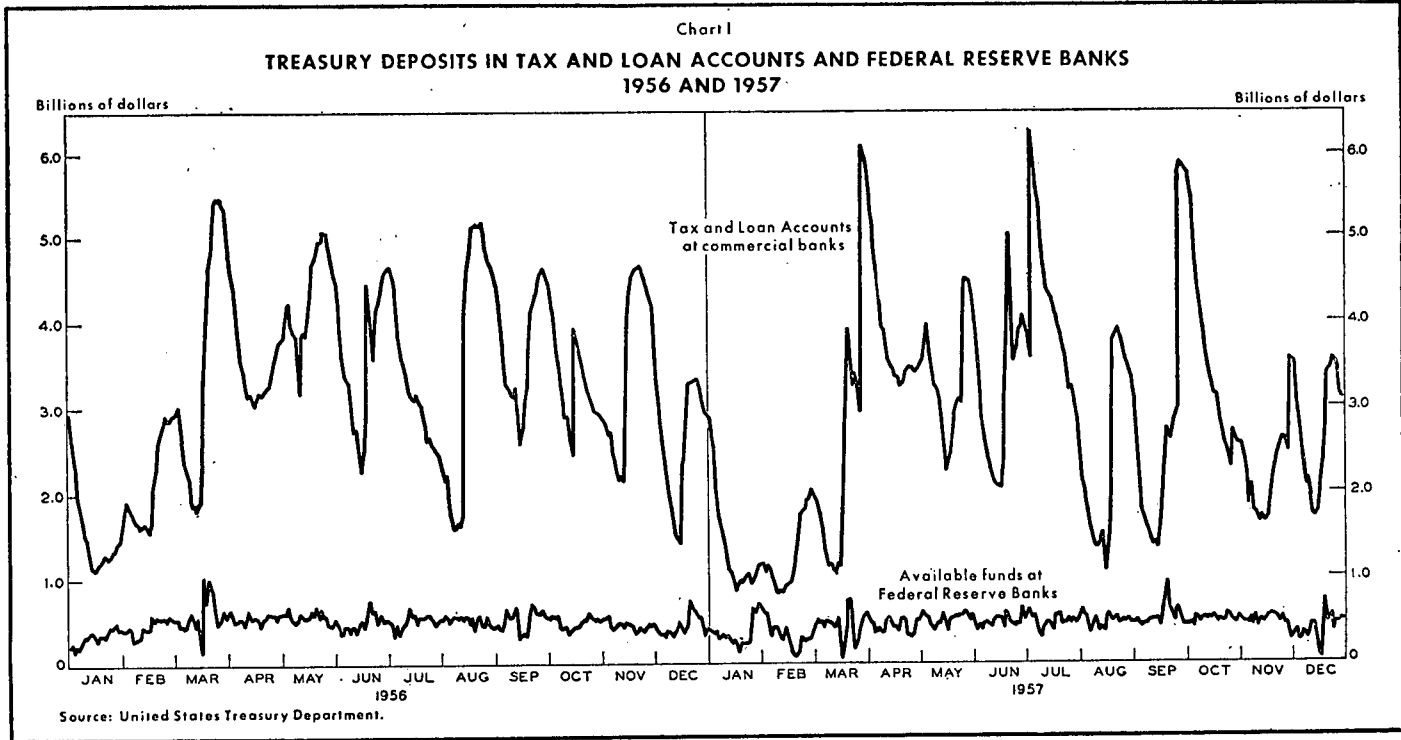
expenditures, tax collections, and debt transactions in certain months and in certain days of each month.

Almost all of the Treasury's cash disbursements are made by checks paid by the Government's fiscal agents, the Federal Reserve banks. Treasury cash receipts, on the other hand, typically take the form of checks drawn against commercial banks. These receipts, reflecting tax collections of the proceeds of securities sales, sooner or later must be funneled through the Treasury's balances at the Federal Reserve banks, to reappear as disbursements. Thus, the flow of Treasury funds from commercial banks into the Reserve banks involves losses in commercial bank reserves, while Treasury disbursements from the Reserve banks produce reserve increases. The method used to minimize the impact of these massive flows of funds into and out of the Federal Reserve banks involves the regulation of the Treasury's balance at the Federal Reserve banks so that it is held as nearly constant as day-to-day operations permit; consequently, temporary accumulations of Treasury deposits are left in the commercial banks. This means that the amounts shifted each day from the commercial banks need to be gaged as closely as possible to the day's disbursements from the Treasury's balances in the Federal Reserve banks. The cycle is completed when the Treasury disbursements from the Federal Reserve banks flow back into commercial bank accounts.

If, in contrast, all tax receipts and the proceeds of Government securities sales were deposited immediately in the Treasury's accounts with the Reserve banks, the effect would be periodic heavy drains on bank reserves, particularly in the quarterly tax months, as funds poured in more rapidly than they were disbursed. The resultant contraction of the reserve base could have seriously disruptive effects on the money market and the functioning of the entire banking system.

An example of the actual variations in the Treasury's deposit balances during March 1957 clearly shows these potential reserve effects. The Treasury's combined cash balances in all depositories (including the Federal Reserve banks) fell from \$2.5 billion at the beginning of the month to \$1.2 billion on the 15th, then rose in 6 days to 4.7 billion on March 21 as a result of the concentration of tax collections, and then dropped away once again, due to net disbursements, to 3.4 billion on March 27. On the following day, a new money borrowing brought the cash balance to \$6.6 billion, and the end-of-month balance was \$6.5 billion. If these large increases and decreases of the Treasury's cash balances had taken place exclusively in its balance at the Federal Reserve, that balance would first have been reduced by more than \$1 billion (with member bank reserves correspondingly increased), to be followed by a 3½ billion increase in the balance; it would then have been reduced again by 1 billion, and finally raised once more by about \$3 billion. Such swings in the Treasury's balance at the Federal Reserve would have meant that the reserve balances of the commercial banking system would have been, successively, raised by 7 percent, cut by 19 percent, increased by 7 percent, and reduced by 17 percent, all within the space of 1 month.

For reasons of operating convenience, but principally to prevent the irregular ebb and flow of Government funds from interfering with the smooth and effective functioning of the Nation's payments mechanism, it has been necessary to develop a set of techniques especially adapted to minimizing the strains and dislocations of drawing money from the commercial banks in which it is held, into the Federal Reserve banks, and later disbursing it. These techniques include handling the bulk of the Treasury's receipts in two steps: (1) Most receipts are credited initially to the Treasury's tax and loan accounts in commercial banks all over the country by transfers from their respective customers' accounts as each bank actively solicits its customers to make their payments due the Treasury through the bank; and (2) through carefully scheduled "calls," the funds in these accounts are transferred, as needed, to the Treasury's deposit balances in the Federal Reserve banks. This procedure for mobilizing the Treasury's funds has been in the course of development since 1917, and makes it possible, even in periods of abrupt shifts in Government receipts and disbursements, to synchronize rather closely the withdrawal of reserves from the commercial banking system with their subsequent replacement through disbursements from the Treasury's Reserve bank accounts. In other words, it enables the Treasury to keep its balance with the Federal Reserve banks reasonably



stable. The present article examines the effective mechanism employed by the Treasury in managing its fluctuating working balances with a minimum of undesirable money market effects.¹

MANAGEMENT OF THE TREASURY WORKING BALANCES

On objective of the "housekeeping" aspect of managing the Treasury's balances is to neutralize the impact of day-to-day operations on commercial bank reserves, and one measure of its success is the restricted amplitude of the daily variations in the Treasury's Reserve bank balance, shown in chart 1. In recent years the acknowledged target has been a balance of \$500 million in the Treasury's combined balance in the 12 Federal Reserve banks and their branches. Experience has shown that an active working balance of approximately this size is necessary to accommodate the Treasury's transactions. Aggregate balances in the commercial bank depositories vary over a range of several billions of dollars because they absorb the wide fluctuations caused by differences in the timing of overall receipts and expenditures.

The Treasury acts in consultation with officials at the Federal Reserve Bank of New York in scheduling "calls" against its tax and loan account balances at the three classes of depositories (A, B, and C).² When regular calls on class B and C depositories are necessary they are ordinarily announced each Monday for payment on the following Friday and Monday, and further calls are announced on Thursday for payment on the following Tuesday, Wednesday, and Thursday. Under this schedule, these depositories are given 4 to 7 days' notice in which to prepare for the impending withdrawal. Treasury calls for the transfer of its balances from the smaller class A banks into the Federal Reserve banks are ordinarily made only once a month and usually on a week's notice. This 1-month interval merely reflects the Treasury's desire to avoid extensive calling for a large number of small amounts. Of course, calls could be made more frequently on these A banks at any time if the Treasury should wish to do so, and on occasion it does.

The total size of each call from the commercial banks must be set in accordance with estimates of how large the cash needs of the Treasury are likely to be. This requires a forecast of the daily receipts and expenditures which flow in and out of the Reserve bank balance of the Treasury. These forecasts are based on detailed studies by both Treasury and Federal Reserve staffs of many individual categories of receipts and expenditures.

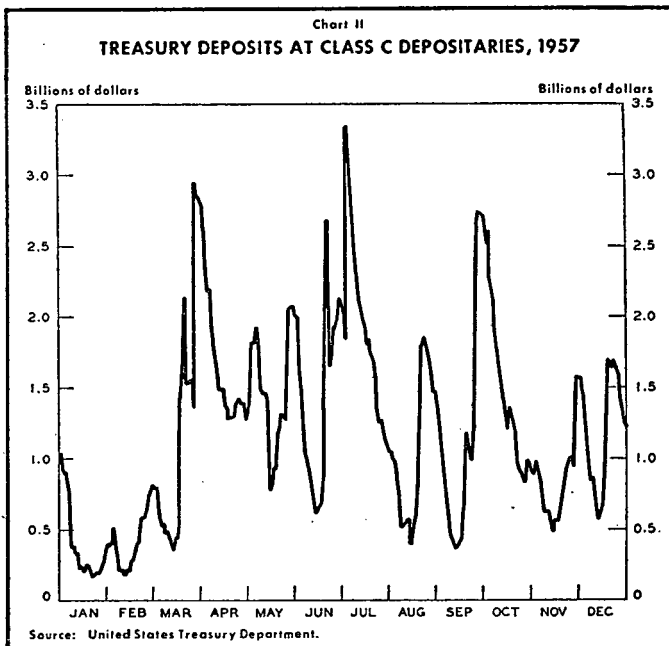
Should actual Treasury receipts and disbursements on the days between the issuance of the regular call and the actual transfer of the funds vary substantially from the forecasts projected at the time of the call, the transfers already scheduled would produce unintended effects on bank reserves by either withdrawing too much or too little from commercial banks. To compensate for such unavoidable forecasting errors, it is necessary at times for the Treasury to make "last minute" adjustments by means of a "special" call on the class C banks or by a redeposit of amounts withdrawn earlier from these banks; deferrals or cancellations of previously scheduled withdrawals from "C" banks are also made.³ Since these are the Nation's largest banks and are, generally, banks that rely daily upon the money market to adjust for large movements of funds, they are able to accommodate themselves to withdrawals or redeposits by the Treasury on very short notice. As a rule, notice is given such banks before 11 a.m. (Washington time) on the day on which the change is to be effective. An indication of the impact of these swings on class C depositories is given in chart II, showing the extremes of daily variation in the aggregate balances at these large banks during 1957.

¹ For a detailed description of the Federal Government's financial operations and their effects on the money market, see "The Treasury and the Money Market," Federal Reserve Bank of New York, 3d printing (May 1956).

² These depositories are classified on the basis of size, and the classifications are periodically reviewed by the Treasury. The most recent review of the roughly 11,000 "special depositories" placed into class A those banks whose Treasury tax and loan accounts were \$150,000 or less on Mar. 19, 1958. Class B includes all bank depositories whose tax and loan accounts exceeded \$150,000 on that date, except for the special group of the largest banks, designated class C. Banks with total deposits of \$500 million or more, as of the latest detailed report on assets and liabilities to the bank supervisory agencies (which is known as a call report), are class C depositories. As of the end of 1957, there were 9,949 banks in class A, 1,319 banks in class B, and 46 in class C. The total tax and loan balances of banks in each of the three classes, as of Dec. 31, 1957, were about \$500 million for class A; \$1.3 billion for class B; and \$1.2 billion for class C.

³ These adjustment procedures were first instituted on July 29, 1955.

The success of this flexible call procedures in avoiding unstabilizing effects on bank reserves is apparent in chart I, which shows the daily fluctuations in the Treasury's deposits in tax and loan accounts and with Federal Reserve banks during 1956 and 1957. In contrast to the wide and irregular swings in the tax and loan balances, the variations in the Treasury's Reserve bank balance were small indeed. Except for brief intervals, the latter balance held within a daily range of \$400 to \$600 million during the period covered by the chart. The tax and loan balances, on the other hand, frequently exceeded \$4 billion and reached peaks of \$5 billion and even \$6 billion which were followed by rapid declines to the \$2 or \$3 billion range. This variability in the tax and loan balances gives an indication of the magnitude of swings in total reserves that might have resulted from the daily routine of the Treasury's financial operations if the special facilities had not been developed.⁴ The small fluctuations in the Treasury's Reserve bank balance around the \$500 million level, on the other hand, indicate the remaining reserve effect that it has not thus far been possible to eliminate. It should be noted that, on the rare occasions when the Treasury's balance with the Federal Reserve banks fluctuated widely from the \$500 million norm, the deviations were permitted by the Treasury in the light of its own needs and in consultation with Federal Reserve officials.



In the final analysis, resort to a special mechanism, such as tax and loan accounts, for easing the shift of reserves from the commercial banking system to the Treasury's Federal Reserve balance is imperative. Under fractional reserve banking arrangements, and with the Treasury receiving funds in varying amounts from depositors in virtually every bank in the country, the absence of such a system would work a kind of capricious havoc upon the reserve position of the banking system as a whole, with undesirable effects in turn on the position of individual banks. As Government receipts and expenditures have grown, country by country around the world, one country after another is becoming interested in the techniques developed here.

⁴ Swings of this magnitude in the tax and loan accounts do not necessarily affect commercial bank deposits as a whole. Unless new money borrowing by the Treasury from the commercial banks is involved, they usually reflect only shifts from private to Treasury deposits in the commercial banks, without affecting total bank reserves in a major way. There is always, of course, a problem for individual banks, as some lose and others gain deposits on balance, but that is a normal occurrence in conducting banking operations.

TREASURY BORROWING AND BANK RESERVES

The cash borrowings of the Treasury introduce a peculiarly destabilizing influence into the banking system. Whereas seasonal concentrations of tax collections may at times generate somewhat larger flows of funds than the amount involved in an "average" cash borrowing, the transfer of taxes takes a number of days, while a cash borrowing usually involves a large shift of funds on a single day. Moreover, cash borrowings by the Treasury may take place rather often since they are not confined to meeting annual operating deficits but are also required—and usually in far greater amounts—to replenish the Treasury's balances during seasonal lows in tax collections and in order to repay matured debt that is not refunded and savings bonds that are turned in for cash redemption. In the calendar year 1957, for example, the Federal Government had a moderate cash surplus, but was nevertheless compelled to raise a total of nearly \$20 billion in new cash (exclusive of the rollover of regular Treasury bills).

The six major cash flotations undertaken last year ranged in size up to \$3.6 billion. In each case, commercial banks were allowed to pay by credit to Treasury tax and loan accounts for their own and their customers' subscriptions, and virtually all of the proceeds were received in that form. If, instead, the Treasury had required direct payment to the Federal Reserve banks, the reserve balances that would have been withdrawn from the banking system on the payment dates for the six flotations would have ranged from about 4 percent to about 19 percent of total bank reserves. And the reserve base would have been subjected to considerable irregular buffeting thereafter, reflecting the release of the borrowed funds in the ordinary course of Treasury disbursements. If the Federal Reserve System were to attempt to cushion shocks of such size to the reserve base, the scale and frequency of its open market operations during each Treasury financing would need to rise far above current requirements for seasonal operations or for implementing changes in credit policy.⁵ With the arrangement for payment through tax and loan accounts, on the other hand, and with the flexibility of the fractional reserve banking system, the immediate impact on the reserve base was restricted in each case to no more than the increase in required reserves to cover the new tax and loan deposits credited to the Treasury. In Treasury borrowings in which the securities were purchased on original issue almost entirely by the banking system, the immediate increase in required reserves over recent years has generally been about one-sixth of the amount borrowed.

Perhaps the most effective method of illustrating the process of credit creation in a Treasury financing is to look at a specific offering and to trace the subsequent cash flows through the tax and loan accounts to the Federal Reserve Banks. The auction of \$3 billion of tax anticipation bills (TAB's) on June 26, 1957, can be used as an example. Since all but \$90 million of this sale of bills was paid for with credits to tax and loan accounts, approximately \$2.9 billion were added to the latter accounts on the July 3 payment date. This peak, somewhat reduced by that day's withdrawals (or calls), is apparent in chart I, and partially in chart II.

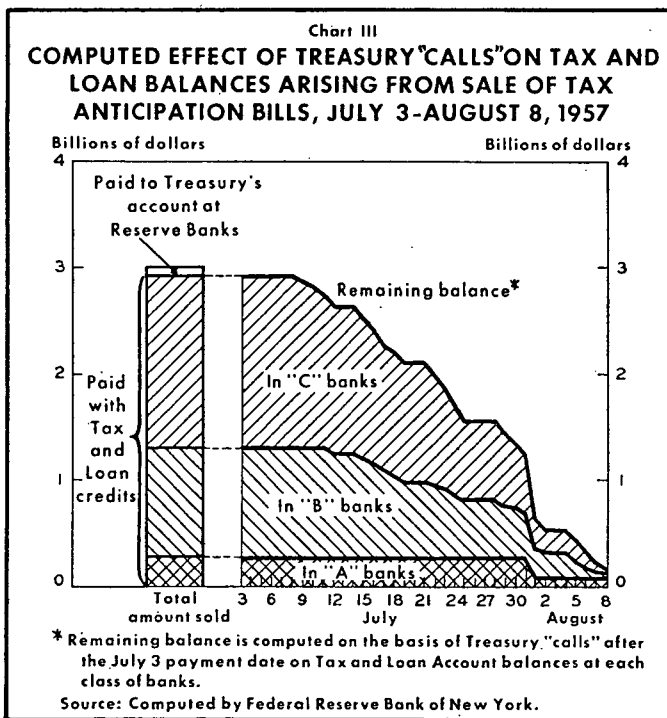
The privilege of paying for the new bills through credit to tax and loan deposits meant that commercial banks, buying the bills for their own portfolios, had an immediate reserve need equal to the required reserves on the new deposits—at that time 20 percent in the case of the New York City banks—whereas they began earning interest on the full amount of their allotments immediately upon issue. However, the Treasury soon issued calls against the new tax and loan account deposits and the bills (or other assets) had to be sold so that funds could be available to pay over to the Treasury's balance at the Federal Reserve banks. Many sales of the new bills were made at a price lower than the original purchase price, but such losses generally were offset by the earnings on the new securities for the period held. In practice, this meant that the commercial banks paid a price at the time of original sale higher than the Treasury could have obtained through the sale of the issue without the privilege of payment through tax and loan account credit. As a result the banks were able to outbid nonbank subscribers for the issue. Yet when nonbank investors first purchased these securities from commercial banks, the price was substantially lower than that in the initial sale by the Treasury.

⁵ For a discussion of the Federal Reserve System's "defensive" and "dynamic" responsibilities for monetary control, see R. V. Roosa, "Federal Reserve Operations in the Money and Government Securities Markets," Federal Reserve Bank of New York (July 1956), ch. I.

This illustration, which refers to the "retailing" of an auction issue, sets forth quite clearly the distribution of possible gains from a Treasury financing, to the Treasury itself, commercial banks, and other investors. In addition, the Federal Reserve System benefited by avoiding large-scale open-market operations that might have confused the market. In the case of coupon-bearing issues offered on a subscription basis such gains are not so clearly ascertainable for illustrative purposes, because coupon securities are sold at a fixed price and not to the highest bidders. The same forces are nonetheless at work.

Whether Treasury flotations carry a coupon, or are sold at auction, bank payments through credit in tax and loan accounts provide a striking illustration of the process of multiple deposit expansion. To validate this deposit multiplication, an increase in required reserves of about one-sixth of the deposit increase has usually been required. If excess reserves at the outset of a deposit expansion are insufficient, these required reserves must be supplied by the central bank. The Federal Reserve System may provide the necessary amount of reserves by open market operations, through the "discount window," or through changes in reserve requirements, the choice of action depending upon the current direction of policy, expected seasonal changes in credit conditions, and other factors.

Returning to the illustration of the sale of TAB's in July 1957, it should be noted that member banks in the aggregate were in a negative free reserve position at that time; that is, total member bank borrowing from the Federal Reserve banks exceeded excess reserves in the banking system. In order to subscribe for the new securities it was necessary for the banks to mobilize a substantial amount of additional reserves, since the required reserves needed to support the increase of nearly \$3 billion in tax and loan account deposits amounted to approximately \$500 million. An examination of the monetary statistics for the period surrounding the Treasury financing indicates that this need for additional reserves was met largely through an expansion of Reserve bank credit. Otherwise, the banks could not have taken up the new issue without making simultaneous reductions in their other loans and investments, with a resulting severe wrench to the availability of credit and the money market. In the week ended July 10, on a daily average basis, the System made open market purchases of about \$230 million and extended \$120 million of repurchase agreements to Government securities dealers, and member bank borrowing increased by about \$150 million.



The net result of the Federal Reserve actions, therefore, was to facilitate the initial placement of this issue with the commercial banks, pending its distribution to others. In essence the banks served as temporary "underwriters." The question of how long to permit the additional Federal Reserve credit to remain within the commercial banking system, once the new securities were firmly lodged in investors' portfolios, was decided in the context of the degree of monetary pressure that was being sought at that time. As it worked out, the additional reserves were soon needed to support a seasonal expansion of the money supply.

The next step in making the proceeds of the sale of TAB's available for financing Treasury disbursements was to transfer the amounts that had been credited to the tax and loan accounts to the Treasury's balance at the Reserve banks. The manner in which this step was carried out is illustrated in chart III. The gradual drawing-down of the tax and loan account balances at the three classes of depositories cannot be determined from any reported data, since the Treasury's calls apply to the total balance in the accounts and not simply to that portion of the balance representing the proceeds of a particular sale of Government securities. The data in the chart were computed by assuming that the calls subsequent to the July 3 payment date had the same proportionate effect on the proceeds of the sale of TAB's as on other balances in the tax and loan accounts.

Withdrawals of balances at C banks, where the largest share of the proceeds accumulated, proceeded at a somewhat more rapid rate than the withdrawals at B banks, and in each of these classes of banks the rate of withdrawals was far more rapid than in the smaller class A banks. In fact, the first withdrawals for the latter did not occur until August 1, or 29 days after the TAB's had been issued. By that date the C banks had already transferred to the Reserve banks almost five-sixths, and the B banks about three-fourths, of their original credits to tax and loan accounts in payment for the new bills. By August 10, or 38 days after the securities had been sold, the calculations in the chart indicate that less than \$200 million remained out of the starting balance of \$2.9 billion.

There is, of course, an element of potential profitability for each depository bank in having tax and loan account balances, however these arise, provided the variations are not so great as to prevent some useful employment of the funds as an offset to the costs of handling credits to the account. Whether it is profitable for the individual bank probably depends, as much as anything, upon the enterprise it demonstrates in handling these funds while assuring the prompt remittance of funds due the Treasury. Whether profitable or not, many individual banks apparently continue to perform these services, both in handling balances and in "underwriting" and distributing Treasury issues of Government securities, because of the obligation which they feel arises from the unique role which commercial banks occupy as a part of the Nation's monetary mechanism. That is, commercial banks are, in a broad sense, special instrumentalities of the U.S. Government in that they exercise in part the function of creating money.

USEFULNESS OF PAYMENT FOR CASH OFFERINGS WITH CREDITS TO TAX AND LOAN ACCOUNTS

Commercial banks acquired virtually the entire issue of TAB's in the July 1957 auction because the privilege of paying through tax and loan accounts made it possible for them to pay the Treasury a higher price than could other direct subscribers, with the result that the net interest cost to the Treasury was clearly much lower than would otherwise have been possible. As noted in the previous section, however, the forces of competition made it inescapable that the banks had to share any of their gains with other investors. Thus the principal net result was the profitability for the Treasury, which actually obtained a net cost for its issue well below the going market yield on comparable securities. On the day of issue, for example, a similar security maturing only a month later than the TAB's (a 3½-percent certificate maturing April 15, 1958) carried a market yield of 3.74 percent (bid) while the TAB was sold at an average price equivalent to a 3.485 percent yield.

The value of the added tax and loan account balance to the individual bank depended upon such factors as the banks reserve position at the time the credit was established, the probable price at which the TAB's would be sold to investors, the net yield the bank was able to earn on additional (or substitute) loans or investments, and the length of time the new deposit in the tax and loan account

remained with the banks. All of these factors had, in some way, to be estimated by each subscribing bank before it could adequately judge the price it could afford to pay or the quantity it would like to have.

In effect, therefore, payment with credits to the tax and loan accounts results in the subscribing banks serving for a time as "underwriters" and distributors for the Treasury. The banks who calculate correctly are likely to find that they are compensated for their service as "underwriters" of the new issue, while the Treasury is able to keep for itself, by borrowing below the market rate, a considerable portion of the possible earnings value of the tax and loan account credits to the banks. The process also provides a good example of the more or less automatic working of competitive forces in the market for Treasury securities.

CONCLUSION

The ability of the Nation's monetary system to accommodate immense transfers of funds within the private sector of the economy without undue strain on the money market is evidence of the system's remarkable flexibility. Transfers between the private and Government sectors raise a special problem, however, because of the unique role of the Federal Reserve banks as the Government's banker. Payments to the Treasury's balance at the Reserve banks involve a loss, and disbursements of that balance a gain, of commercial bank reserves, with potentially magnified effects (under our fractional reserve system) on the availability of bank credit.

Given the impossibility of maintaining an even balance each day between the Government's total receipts and disbursements, the Treasury must employ a financial mechanism which avoids large and sudden increases or decreases of the commercial banks' reserve base. The system of tax and loan accounts is that type of mechanism. As reservoirs for temporary accumulations of Treasury funds, these accounts provide a necessary buffer against the disturbing effects of massive movements of funds during Treasury financings, or on the major taxpayment dates. Moreover, the tax and loan account mechanism facilitates monthly collection of withheld and social security taxes, thereby giving the Treasury the proceeds ahead of the quarterly tax returns. By spacing out the transfers of funds into its Reserve bank deposits, the Treasury aims to achieve a close balance between the inflows and outflows, with the result that these deposits are held at a fairly steady level. Experience has shown that this method of managing the Treasury's balances is well adapted to the U.S. banking system and that it can be used successfully to avoid the grave money market disturbances that might otherwise be a mechanical byproduct of large-scale Treasury operations.

Question 2.—If the commercial banks are not to pay interest on Treasury accounts, why should not these funds be drawn properly back into the Federal Reserve, which could invest them in short-term Treasury bills until the Treasury drew upon the Federal Reserve?

The Treasury maintains balances in tax and loan accounts with commercial banks so as to avoid the disruptive effects on the economy and to the banking system which would occur if the large amounts of cash collected from time to time by the Treasury from taxes or from the sale of public debt obligations are withdrawn at one time and paid into the Federal Reserve banks.

Any action which would have for its purpose the withdrawal of these funds from the commercial banks and their deposit in the Federal Reserve banks ahead of the time when they are needed to meet expenditures of the Government for the purpose of investing them in short-term Treasury bills would give rise to the disruptive effects which the Treasury seeks to avoid by keeping the funds on deposit in Treasury tax and loan accounts in the first instance. When funds are withdrawn from the commercial banks and paid over to the Federal Reserve banks in order to build up Treasury balances in the Reserve banks, the commercial banks have to find free reserves to cover these payments.

There are only two ways in which the commercial banks can do this when their funds are fully employed (when they have no excess reserves). One is to reduce assets, which can be accomplished either by selling securities in the market (or cashing them in at maturity) or by terminating loans; the other is to increase liabilities by borrowing from the Federal Reserve banks. Commercial banks generally prefer to reduce their assets rather than to be in debt to the Reserve banks.

It is true that if the Federal Reserve purchased securities from the banks simultaneously with the movement of deposits out of the banks this would keep the commercial bank system as a whole in equilibrium at the lower level of deposits (and reserves). In theory, at least, the suggestion would appear feasible. If there was only one bank it might work (although still with disadvantages to be pointed out later), since the transactions would in fact be simple and instantaneous. It might even work if only a dozen or less banks were involved, as in Canada and the United Kingdom. But its operation through 11,000 individual banks would present serious obstacles.

The magnitude of Treasury operations in tax and loan accounts is so large and the number of banks so great that the effect of timing and the effect among individual banks would be very disruptive to the money market. In the first place, even if it were possible to do the entire operation within a day or two there would necessarily be a difference in timing between the flow of reserve funds out of the commercial banks and the return flow due to Federal Reserve purchases of securities. When the flow is reversed as when the Federal Reserve sold securities as the Treasury made disbursements and the funds flowed back into commercial bank reserves the same problem of uneven timing would arise. In the second place, it is obvious that in the case of an individual bank the funds would not flow back in even approximately the same proportion as they were withdrawn, even if timing were perfect for the banking system as a whole.

At the peak of each of these flows of funds, Federal Reserve credit would be expanded by the amount of Governments they acquire. This expansion, even though offset by increased Treasury deposits with the Federal Reserve, rather than by increased bank reserves, would still be widely interpreted as an inflationary step simply because Federal Reserve credit had grown. Any lack of precision in offsetting the flow of funds away from and back into member bank balances as the Treasury's balances with the Federal Reserve rose and fell would also produce unforeseen contraction or expansion of bank reserves.

The job of trying to estimate each day's flow of funds accurately enough to permit an operation such as this to proceed smoothly would be almost impossible, quite apart from the tremendous disparity of effects from one bank to another. Seemingly small shifts in the reserve position of the banking system (sometimes only \$50 or \$100 million) can affect short-term interest rates through the normal operation of Federal funds. The ability to keep these shifts sufficiently small would be greatly weakened if the suggested procedure were followed, with correspondingly greater risk of wider short-term interest rate fluctuations and the possibility of disorderly markets.

Unless the Federal Reserve makes sure that sufficient excess reserves are provided, it is also very difficult to see why a commercial bank would have an incentive to buy any new Treasury securities under such circumstances—either for its own account or for customers—since the resulting deposit would be withdrawn immediately and the bank would be forced to sell either the new issue it just acquired or something else. Bank underwriting and secondary distribution of new Treasury issues would be seriously undermined unless the Treasury took alternative steps such as (1) paying commissions to the banks, (2) adding materially to the interest rate attractiveness of new issues, or (3) increasing the frequency (and cutting the size) of its offerings so that money was borrowed in amounts intended to cover the expected cash outflow for the ensuing day or 2 days (or a week at the most) on a hand-to-mouth basis. All three of these alternatives would add significantly to Federal borrowing costs.

Question 3.—If the deposits are to be maintained in commercial banks, could not the Treasury work with a smaller balance and handle temporary surges or shifts in cash position by an increased use of its authority to draw temporarily on the Federal Reserve banks?

The Treasury always endeavors to maintain its aggregate balances in tax and loan accounts at minimum levels consistent with the needs of the Treasury for funds to meet the day-to-day and month-to-month operations of the Government. It is not possible to maintain these balances at a constant level. The tax and loan accounts serve as an equalizing reservoir between the inflow of taxes and borrowing proceeds on the one hand and disbursements on the other.

It is necessary for the Treasury to borrow funds at times when the market is receptive to borrowing, and this affects both the amount and timing of new issues as well as their cost.

Also, tax collections flow into the Treasury's balances on a very uneven basis. In some months of the year, total tax collections are four times as great as tax

collections during other months. Furthermore, tax collections during the course of the month may vary greatly from week to week and from one day to another. Expenditures follow a more even course, but even here short-term fluctuations are important and not always predictable. All these are factors which account for the great variations between low and high balances in the Treasury's tax and loan accounts during the course of a month or a year.

These shifts in the timing of receipts and expenditures should not be met by resorting to direct borrowing from the Federal Reserve banks except for rare use as a supplement to the present system when there is a particular strain before peak tax payment dates or when an unexpected volume of debt repayments must be made in cash.

The Treasury's direct borrowing authority with the Federal Reserve provides an essential emergency "line of credit" which the Treasury can tap. It may use this authority when day-to-day cash flows are out of line with estimates and the resulting cash balance is below minimum operating levels. It also needs such authority in order to meet any sudden nationwide emergency which would require heavy cash payments from the Treasury before public debt obligations could be sold to the public to provide such funds. The availability of this direct borrowing authority permits the Treasury to operate on a smaller cash balance than would otherwise be possible, with corresponding savings to the taxpayer. The Treasury's policy has always been to use this borrowing authority sparingly, and only on a temporary basis, since we recognize that selling obligations of the Government directly to Federal Reserve banks creates high-powered money and tends to be inflationary.

Even under conditions when the creation of Federal Reserve credit is completely offset by a Treasury deposit rather than by increased bank reserves it establishes an unwise precedent. History is full of instances in other nations where direct borrowing by the Treasury from the central bank has been the forerunner of disastrous inflationary consequences.

Quite apart from the question of possible misuse (or misinterpretation of the use) of the borrowing authority it is clear that the objections raised to widely fluctuating Treasury balances in Federal Reserve and widely fluctuating private balances in commercial bank accounts in the answer to question 2 are also applicable here. The avoidance of the tremendous drain on commercial bank reserves accompanying the withdrawal of customers' balances when they pay their taxes or purchase securities, and the tremendous resurgence of deposits as Treasury expenditures flow through the banking system is one of the major functions of the Federal Reserve System, and it is a function which is being performed quite successfully. To accept gyrations in a magnitude not even dreamed of when the Federal Reserve Act sought to achieve a smoother flow of funds throughout the banking system would seem, therefore, to be a serious step backward.

It is also unclear what this suggestion would accomplish as a practical matter. In the first instance the Treasury would borrow \$1 billion from the Federal Reserve, let us assume, and Treasury's deposits with the Federal Reserve would be increased correspondingly. This is simple, but the reverse of the transaction is much more complicated. As the Treasury spends the money it draws checks on its balance in the Federal Reserve banks. Those checks are then deposited by the recipients in the commercial banks, with a corresponding increase in bank reserves (let us assume one-sixth required reserves and five-sixths excess reserves). There would obviously be a large expansion of bank credit if the process stopped here.

To counteract this the Federal Reserve, therefore, simultaneously sells securities to the banks to absorb what would otherwise be excess reserves. This can be done directly, or it can be done indirectly by the Treasury's selling new securities to the banks and paying off its debt to the Federal Reserve. The net effect is the same in either event. As a matter of fact, the net effect of the whole transaction is the same as in the case of the procedure the Treasury follows now when it borrows from the banks. The suggested transactions with the Federal Reserve are merely superimposed on them. However, any error in estimating the timing of transactions to offset the creation of bank reserves would, again, have the effect of restraining or easing credit accidentally.

Any intention implicit in this suggestion that somehow Treasury borrowing costs would be reduced by shifting Government security holdings (and earnings) from commercial banks to Federal Reserve banks for short periods of time seems very unlikely to occur. Banks would find their present incentive to do a good underwriting and secondary distribution job on new Treasury securities ser-

iously curtailed if deposits are kept extremely low. The Treasury then has the choice of paying correspondingly higher interest rates to attract the banks (always assuming, of course, the maximum Treasury effort to borrow outside of banks) or the payment of commissions, with a net result likely to be higher rather than lower interest costs to the taxpayers.

Question 4.—Would you agree that the law is now obsolete and should be repealed which prohibits commercial banks from paying interest on demand deposits?

The law which prohibits commercial banks from paying interest on demand deposits was enacted in the early 1930's to correct abuses in the banking system which had grown up prior to that time. When commercial banks were permitted to pay interest on demand deposits, there was a tendency for banking funds in the smaller cities and rural areas to be drained away from those banks into the larger commercial banks in the principal money centers. Banks competed aggressively for those deposits and paid higher and higher rates of interest to attract them.

As a result, banks were under pressure to make more loans and investments to earn enough to pay higher rates, even though the quality of many such marginal loans and investments became more and more substandard. Consequently, during the depression of the early 1930's this increased the banking difficulties that occurred at the time. It was that situation which caused the Congress, in the Banking Act of 1933, to provide that commercial banks could not pay interest on demand deposits.

In the public interest, there are two reasons why the Treasury believes banks should not pay interest on such deposits. In the first place, the competition between banks for demand deposits does not create any additional deposits. The aggregate amount of demand deposits in the commercial banks is largely controlled by the Federal Reserve through the operation of monetary policy. Therefore, the effect of competition is to shift deposits between banks. On the other hand, member banks are permitted to pay, at present, as much as 3 percent interest on savings and time deposits (unless State laws specify a lower maximum), but the payment of interest on these deposits has an economically desirable effect by increasing incentives to save. The different character of time deposits is not only reflected in the fact that a bank does not have to pay them on demand, but also because of lower reserve requirements for them and the longer term nature of the assets generally held as an offset to them. In the second place, if the banks were to bid competitively for demand deposits because of this added interest expense, they would probably find it necessary to charge generally higher interest rates on loans or exact higher service charges, or both. Even if the Federal Reserve and the Federal Deposit Insurance Corporation could by law be authorized to set maximum rates on demand deposits—as is done now on time deposits—these influences would be moderated, but not eliminated.

The payment of interest on tax and loan accounts would probably add to Treasury borrowing costs. The present practice of commercial bank payment for new Treasury issues through tax and loan accounts is very effective in stimulating the banks' interest in Federal securities, not only for their own accounts, but also as distributors of these securities in the secondary market. To the extent that banks are required to pay interest to the Treasury on each additional amount of tax and loan account they acquire, this obviously will be reflected in the price they will be willing to bid for securities they purchase from the Treasury at auction as well as affecting the coupon rate which the Treasury would put on its fixed-rate securities (certificates, notes, and bonds).

The point should also be made that there are some commercial banks in this country which do not even accept savings or time deposits at interest, so they would be even more unwilling than the average bank to pay interest on Government demand deposits. In addition, there would unquestionably be a considerable number of other banks which would not think it was good business to accept Government deposits with their extreme volatility if they had to pay interest on them. Payment of interest on all demand deposits would also make them more attractive than now for nonbank investors to hold, tending to increase interest rates which the Treasury and all other borrowers would have to pay to compete.

As mentioned in answer to question 1, the initiation and maintenance of an adequate service charge or fee system that would presumably grow out of a requirement of interest on demand deposits would be difficult. No one can predict, of course, what arrangement of fees and interest rates would be developed

if such a system were tried. It is quite doubtful, however, if only because of the overhead expenses for both the banks and the Treasury that would be involved in administering such a system that neither the public interest nor the interest of either the banks or the Government would be served. The present system not only dispenses with this unnecessary overhead but also recognizes the fundamental fact that it is difficult to put a price tag on intangible benefits which the Treasury now receives.

I would say this to the Senator at this moment: The Comptroller General has asked that we undertake a study of the problem of charging interest on some of our deposits and the problem of bank service charges to cover their costs on what they do for us.

The CHAIRMAN. I have done that for years, to no avail; absolutely no avail.

Secretary ANDERSON. I know, sir. We are now preparing a study of this sort, and we are going to undertake it. When we undertake it, we will, of course, make available to the Senator the very things you are asking.

The CHAIRMAN. Mr. Secretary, we all have had some experience in State and local governments and State and local politics. We know that one of the chief sources of illicit influence in the States is in the interest-free deposit of balances of local, county, and State governments. I do not know of a State in the Union where there is not either an open or a hidden scandal. There may be such.

We have huge amounts of Government money lying around in the banks upon which no interest is being paid, although these amounts stay there in banks for substantial periods of time and are never drawn upon.

If these minimum deposits either could be put directly to drawing interest or transferred to the reserve, where they could be invested in short-time Government bills, which are highly liquid, and upon which interest could be paid, we could have at least \$100 million a year, in my judgment.

Representative PATMAN. Probably three times that much, Senator.

The CHAIRMAN. Well, I want to be conservative.

And that would help enormously not only in financing the Government, but in its debt problems.

Frankly, I can understand how this developed during the war, when the banks performed a large number of unpaid services to the Government, particularly in the selling of E bonds, and so on. But these unpaid services have diminished in volume, and I think this is largely a bonus—a subsidy to the banks.

Since the banks do not believe in subsidies for others, I think they should join us in trying to remove this subsidy.

Secretary ANDERSON. As I have indicated, Senator, we are going to undertake a comprehensive study of this subject. I should point up that it is my judgment the banks are still providing a number of services, among them being such benefits as the intangible benefits of acting as the secondary distributor of a large volume of securities—both marketables and savings bonds—on which there are no commissions paid, and certain other services which will be elaborated on in the study. On these services it seems to me that one finds it difficult or impossible to put a dollar value. Nevertheless, we will draw up, we are drawing up now, the techniques we intend to employ in making a study of it. We want to have those techniques approved by the Comp-

troller General. Then we will make the inquiry, and the results of that inquiry will be made known.

The CHAIRMAN. I appreciate your doing this. It almost convinces me that the constant importunity of Senators may have some effect. I have almost despaired of this, but I am beginning to get a little hope—not much, but a little.

Congressman CURTIS.

Representative CURTIS. I just want to say that I join the Senator in the request and that I have been very much interested over a period of time in it. So add to that, "House Members."

The CHAIRMAN. I do not want to pose as the only virtuous man on the committee.

Representative CURTIS. I do not know whether we will get anywhere on it, but I want to be sure whether the Senator included with this not just the Treasury fund itself, but also a lot of Government funds that are in the hands of other Government agencies. One thing that has concerned me a little bit on these deposits is that there seems to be a policy measure whereby, in some instances, the State authorities actually designate the placing of these deposits, rather than the Federal agency that actually has the money.

The CHAIRMAN. These are some of the skeletons in the closets all over the country.

Representative CURTIS. I could not agree more.

Secretary ANDERSON. This distinction ought to be pointed out in the case of States and our own operations, Senator Douglas, that in the case of States, various State agencies are putting money into banks. The way the money gets into the bank, as far as the Federal Government is concerned, is that they buy a security and create the deposit or sell a security to a customer and transfer a deposit. So it is not the same thing as our going out to select a bank and say we are going to put so many dollars in the bank.

The CHAIRMAN. They can use that deposit to buy more Government short terms, so they get double interest.

Secretary ANDERSON. I simply wanted to make that distinction. They do not get double interest, however.

Representative PATMAN. Mr. Secretary, I want to ask you a question concerning these withholding taxes. It has been the policy of the Government, under both administrations, to make it easy for corporations and people who are going to be large income-tax payers, to buy short-term securities, and even maturity dates are guided by what will be most convenient to them. Do people whose taxes are withheld get any benefit of any kind for the prepayment of their taxes?

Secretary ANDERSON. I am not sure that I understand the question.

Representative PATMAN. Twenty percent of a worker's salary is deducted each payday, commencing January 31, and for each of the 12 months. If we are going to make it convenient for the larger taxpayers to get some interest income on the money they are holding to pay taxes, should we not also consider making it just a little easier for the person who pays in advance?

Secretary ANDERSON. I would have to study it to see.

Representative PATMAN. I understand. It is not exactly related. But since we are tailoring these securities so that the large income-tax payers will get some benefit when they hold their money back to pay their income tax—

Secretary ANDERSON. Frankly, the question has not occurred to me, but I will pursue it and give you a statement.

Representative PATMAN. I am not trying to dig up any snakes to kill. I am just asking you.

Secretary ANDERSON. I understand.

(The written statement referred to above follows:)

Taxpayers subject to the individual income tax are required by law to pay their taxes more currently than is the case with corporate taxpayers. A large proportion of individual income taxes are, of course, withheld at source, and the remainder of individual income tax receipts come in through current quarterly declarations or through final payments the following April. Most corporations, on the other hand, even with completion of the speedup in corporate tax collections provided by the Revenue Code of 1954, will still be paid equally in the 9th and 12th months of the year of liability and the 3d and 6th months of the following year, rather than earlier.

As a direct outgrowth of the taxpayment schedule provided by law, therefore, a substantial need arises for corporations (and upper income individuals to some extent) to invest short-term funds as they accumulate the money necessary to meet these taxpayments. The need to accumulate funds specifically for tax purposes is recognized particularly by corporations who will accrue their tax liabilities as they are incurred throughout the year and frequently set up reserves for this purpose.

These reserves may be left on deposit with a bank or they may be invested in U.S. Government securities, or in other short-term paper. In the Treasury's efforts to rely on nonbank ownership of the debt insofar as possible we, of course, encourage corporations to invest these funds in Government securities. The Treasury similarly encourages individuals to buy short-term Governments for the same reasons. We know that individuals are much less interested in doing this, however, because the amount of their unpaid liabilities is quite small in comparison with corporations (the effect both of withholding and more current payments), and because they are much less likely to set up specific reserves for tax purposes since they are not business enterprises.

A taxpayer who wishes to invest short-term tax reserves in Government securities may, of course, buy any one of a number of available issues, either in the market or directly from the Treasury. As early as the summer of 1951, however, the Treasury began to offer tax anticipation securities designed particularly for those corporations and individuals who wished to plan their tax reserve accumulation more precisely. These tax and savings notes which the Treasury had on continuous sale from August 1941 through October 1953 were nonmarketable, and owners turned them in at redemption values specified on the security itself. Beginning in 1951, following the enactment of the Revenue Act of 1950 which inaugurated the shift of corporation taxpayments to a more current basis, the Treasury also began to sell marketable tax anticipation securities. These have now entirely replaced the nonmarketable tax and savings notes which were well suited to Treasury needs during the war and early postwar period, but which became inappropriate when short-term interest rates fluctuated more widely.

Taxpayers have found tax anticipation securities a more convenient form of investment than other Treasury issues in most cases because they may be turned in directly at par in payment of taxes. Other Treasury issues usually would either have to be sold in the market or, in the case of regular Treasury bills maturing before a tax date, turned in to the Treasury for cash at maturity, so that funds would be temporarily uninvested. There are no restrictions as to who may buy tax anticipation securities so individuals, as well as corporations, are free to buy them. As mentioned earlier, however, individuals have relatively little interest in accumulating tax reserves because of the basic structural differences between the individual and corporate income taxes.

If the Treasury did not issue these particular securities for purchase by these taxpayers, it would have to issue other securities in lieu thereof, because the Treasury issues public debt obligations only when it is necessary to raise cash to meet its operating requirements or to refund outstanding securities. The Treasury simply borrows from these taxpayers in advance of the due dates on which their taxes are payable, and consequently has to pay interest for this privilege. The borrowings are repaid, in effect, when the taxes are payable.

From the Treasury's standpoint the popularity of tax anticipation securities helps to reduce dependence on borrowing from the banks as well as to provide an excellent way of meeting a large part of Treasury seasonal borrowing needs. Corporations would probably put considerable amounts of their tax reserves in regular issues of Treasury bills even if tax anticipation securities did not exist. However, the convenience attached to the tax anticipation securities has added to their attractiveness and this has helped the Treasury manage the debt more efficiently.

Representative CURTIS. Mr. Chairman, Senator Douglas was so kind as to refer to the very able staff of the Republican committee, and I want to put one thing in the record at this point. This is work by the U.S. Senate Republican policy committee, and has to do with interest payments in proportion to the total economy, pointing out that interest rates by the Federal Government have not increased any more than anything else in the economy. Net interest paid by the U.S. Government is a smaller percentage of gross national product now than at any time under the Truman administration years of "easy money" and inflation. It shows that tables from 1946 to 1957, and I have incorporated the figures for 1958.

May this be included in the record.

Representative PATMAN. Without objection, it is so ordered.
(The material referred to follows:)

INTEREST PAYMENTS IN PROPORTION TO THE TOTAL ECONOMY

Interest payments by the Federal Government have not increased any more than everything else in the economy. Net interest paid by the U.S. Government is a smaller percentage of the gross national product now than at any time under the Truman administration's years of "easy money" and inflation.

[In millions of dollars]

	Net interest paid by the Federal Government	Gross national product	Net interest paid by the Federal Government as percent of GNP
1946.....	\$4,170	\$210,700	2.0
1947.....	4,167	234,300	1.8
1948.....	4,264	259,400	1.6
1949.....	4,400	258,100	1.7
1950.....	4,509	284,600	1.6
1951.....	4,709	329,000	1.4
1952.....	4,729	347,000	1.4
1953.....	4,846	365,400	1.3
1954.....	5,006	363,100	1.4
1955.....	4,320	397,500	1.2
1956.....	5,238	419,200	1.2
1957.....	5,632	440,300	1.3
1958.....	5,300	440,000	1.2

Source: Office of Business Economics, U.S. Department of Commerce, "U.S. Income and Output." Percentages computed.

Representative CURTIS. I wanted to demonstrate a sample of the good work of the committee.

Representative PATMAN. You mean the good work on the interest rates.

Representative CURTIS. No; the accurate economic statistics it gets up.

Representative PATMAN. Of course, I am not accepting that as a good defense of the high interest rate policy.

Are there any other questions of Secretary Anderson?

(No response.)

Representative PATMAN. At this point in the record, without objection, the joint statement of Secretary Anderson and Chairman Martin will appear in the record.

(The materials referred to are as follows:)

JOINT STATEMENT RELATING TO THE TREASURY-FEDERAL RESERVE STUDY OF THE GOVERNMENT SECURITIES MARKET BY ROBERT B. ANDERSON, SECRETARY OF THE TREASURY, AND WILLIAM MCCHESENEY MARTIN, JR., CHAIRMAN OF THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

(Presented for the record in connection with Secretary Anderson's appearance before the Joint Economic Committee, July 24, 1959)

The objectives of national financial policy as pursued by both the Treasury and the Federal Reserve System have meaning, of course, only as they contribute to the sound functioning of our Nation's economy. For our economy to remain healthy and growing, market mechanisms must perform their essential function of providing a meeting place where the forces of supply and demand can operate to achieve the best utilization of resources. One of the problems which has constantly confronted us as a Nation has been how to protect freely competitive markets from forces which would hamper or restrict the performance of this essential function. Only as everyone concerned remains alert to new developments in marketing techniques and organization can we be assured that distortions and restrictive practices have not crept in, to the detriment of healthy growth. This is, of course, just as important and necessary in the financial sector as it is in other areas of the economy.

Developments in the Government securities market a year ago led the Treasury and the Federal Reserve System to undertake a joint study of current techniques and organization in that market. This joint statement is devoted to a discussion of the progress of the study thus far.

OBJECTIVES AND CONDUCT OF STUDY

The immediate background of our joint study was the wide and rapid price fluctuation in the Government securities market during the economic recession and revival of 1957-58. These market movements were naturally a matter of concern to the Treasury in view of its debt management responsibilities. They were of equal concern to the Federal Reserve because of its responsibilities for overall credit and monetary conditions.

In undertaking the study our purposes were to find out how organization and techniques in the Government securities market might be improved, and by what means the danger of future speculative excesses in this market might be lessened. The first step, we felt, was to provide the widest possible basis of factual information. Accordingly, we undertook a detailed and analytic study of the underlying causes of the 1957-58 movements. At the same time we undertook a broad reexamination and reconsideration of the market's general organization.

While experience of the Government securities market during a particular recent period thus provided a specific occasion for initiating this special study, both the Treasury and the Federal Reserve have recognized for some time the need for such a study. The last such study, with somewhat more restricted objectives, was made in 1952 under the auspices of the Federal Reserve's Open Market Committee. The Treasury did not participate in that study since it was primarily concerned with the interrelationship of the market and Federal Reserve operations. Since that time there have been many new developments in the market's machinery and practices, and both the Treasury and the Federal Reserve felt that these developments needed careful evaluation.

The published version of our study will consist of three parts. Part I, which is being made available for public release next Monday, consists, first, of a summary of informal consultations—some conducted in person and some through written communication—held with informed observers of the Government securities markets and important participants in that market. Part I also includes a special technical study of the possibilities of an organized exchange, or auction market, to take care of the major part of the huge volume of Government securi-

ties transactions. These are handled at present, as you know, in the over-the-counter or dealer market, where more than \$1 billion of transactions are handled in a typical trading day.

The informal consultations represented one of the major phases of our study program. These consultations had three objectives: First, to obtain informed impressions and judgments on basic causes of last year's market experience, especially toward midyear and after; second, to find out how market observers and participants viewed and appraised existing market processes and mechanisms; and third, to get the benefit of whatever suggestions might be made for improving and strengthening the market. While our consultations were limited by the special purposes of the study to those who were thoroughly acquainted with market practices, our aim throughout was to seek out the means whereby the Government securities market could function best in the public interest. In our inquiry the needs of the small buyers and sellers were considered carefully, along with those of the Government and of institutional and other large investors.

Consultants included various officials of large commercial banks, of insurance companies and savings banks, and of investment banking firms; primary dealers and intermediary brokers in the Government securities market; financial officers of several large nonfinancial corporations; a number of members and officials of the New York Stock Exchange; a group of financial economists; and a group of academic economists. In all, approximately 75 persons participated in individual or group consultation and about 30 others provided written comments. The individual and group consultations were held in Washington, D.C., and in New York City, and each lasted from an hour to a full day. The discussions with financial and academic economists were on a panel basis, but the remaining consultations were held separately on an informal basis with one or more individuals from a single organization.

Part II of our study is a factual analysis of the performance of the Government securities market from late 1957 to late 1958. Rapidly changing market conditions in this period presented an unusually wide range of problems. To obtain the most complete information possible on the market forces at work, special questionnaire surveys were addressed to all major lenders and participants in the market. On the basis of the answers received, we were able to compile much new data relating especially to market developments from spring through early fall of 1958.

Concerning this second part of the study, it is gratifying to report that the responses to our detailed requests for new statistical information were exceptionally good—indeed, virtually 100 percent.

Part III of the joint project consists of four supplementary and technical studies growing out of the suggestions and findings of the first two parts. We comment later on their particular focus and scope. Neither part II nor part III has been printed as yet, but both are being made available in preliminary form also for release Monday morning.

Before turning to the substance of the entire study itself, a word should be added about how the project was staffed. Both the Treasury and the Federal Reserve System assigned to the study senior personnel experienced in the observation and analysis of the Government securities market. In addition, the Treasury retained the services of a former staff official, having both debt management experience in the Treasury and practical experience in the market, as technical consultant on the study. Federal Reserve personnel were drawn mainly from staffs of the Board of Governors and the New York Federal Reserve Bank, but selected personnel from other Reserve banks also shared in the work. A central Treasury-Federal Reserve staff group was given full responsibility for carrying out the project, and since early spring the members of this group have devoted a major share of their time to it.

INTERPRETATION OF THE 1957-58 MARKET EXPERIENCE

As noted earlier, our study of the Government securities market was focused on the wide swings in market prices and yields of Government securities from late 1957 through the fall of 1958, with special attention paid to the mid-1958 market experience. Through systematic reexamination of available data and the development of new data, we endeavored to find out what lessons could be derived from this experience which would be of benefit to investors generally as well as to those who are responsible for fiscal policy, debt management policy, and monetary policy.

We have not had sufficient time as yet to make a complete evaluation of all the data which have been brought to light by the joint study. Four general observations relating to private investment and credit extension, fiscal policy, debt management, and monetary policy, however, are pointed out by the staff group, as follows:

First, for purchasers of marketable Government securities and for lenders, the risks of speculation on anticipated cyclical price movements of fixed-income Government securities, and particularly of speculation on slim margin, credit-financed holdings, have been widely learned.

Second, in the area of fiscal policy, there is the problem that recession deficits often run to very large size and are delayed beyond the turn in the economy; as a result, they provide stiff financing competition when growing demands for the financing of recovery must be satisfied from a more slowly growing savings supply, and this competition for savings funds may have significant, but largely unavoidable, effects on securities prices and interest rates.

Third, in the area of debt management, there is the problem as to whether, in periods when easy credit conditions lend investor favor to longer term, higher yielding issues, a large and rapid shift in the maturity structure of the debt may result in supply and demand distortions, which may later have upsetting and disruptive effects on the market.

Fourth, in the area of monetary policy, there is the problem as to whether easy credit conditions and accelerating monetary expansion for countercyclical objectives may be carried to the point where banks and other lenders respond too actively to speculative demands for credit, so that lenders, in their zeal to keep their funds employed to fullest advantage, may too easily relax the credit standards which long experience has taught to be sound.

These broad conclusions arising out of our study point up a major financial dilemma which is faced in coping with recession in a free enterprise, market economy.

We all agree that reduction of economic instability is one of our major objectives. National financial policy—which refers to fiscal policy, debt management policy, and monetary policy in combination—is the primary means available to the Federal Government for cushioning recession and stimulating recovery.

Yet, the vigorous use of financial policy to promote economic stability runs the risk of being accompanied by instability in the financial markets, where flexible movement is an essential part of market mechanism. This appears to be a risk which we must take, while doing everything we can to minimize the incidence of instability in these markets.

We know, of course, that many difficulties arise in the effective use of fiscal policy in recession. Deficits in recession are incurred either automatically because of reduced tax receipts and increased social insurance payments or because of specific public policy actions taken to combat recession. These in turn have a direct impact on the prices of Government securities.

The additional burden of increasing debt in such periods—particularly when preceded by inadequate budget surpluses for debt reduction during the preceding rise in the economy—may also have a psychological effect on investors. This may be expected because of the fact that investors are concerned about future budgetary policies as well as the size of the particular financing needs of the moment.

There are other perplexing dilemmas in periods of general economic instability which arise from the very flexibility of our market mechanisms. Investors, for example, are faced in recessionary periods with either keeping their funds highly liquid (with low earnings) or attempting to obtain higher yields available only on longer term investments and thus sacrificing liquidity. Concentration on liquidity would, of course, accentuate recession tendencies, while emphasis on higher yields would help to counteract such tendencies.

The Treasury faces difficult choices during a recession. The orthodox theory of debt management emphasizes short-term financing when resources are not fully employed. At such times, however, the long-term market is receptive to offerings—perhaps for the first time since the middle part of the previous upswing in the business cycle. When the Treasury enters such a period with a large and growing floating debt, it would seem advantageous to refinance some part of this debt at longer term. Such a course is also desirable to provide greater leeway in choosing financing alternatives when the recession-induced deficit is sooner or later encountered. And since a recession deficit when it occurs must be financed within a relatively short period of time, the Treasury must look forward to making heavy calls on available savings during the deficit-

financing period. In the second half of 1958, for instance—a recovery period, but one coinciding with heavy deficit financing requirements—the Treasury was obliged to absorb the equivalent of a third or more of the total new savings funds then available. The Treasury's problem of maintaining a debt structure adaptable to changing circumstances without itself contributing to instability of the economy is a formidable one.

Monetary policies, if they are to contribute to resolving our problems of general economic instability, must be deliberately and appropriately adjusted to combating recession and they must be shifted when an upturn is evident. The timing and extent of monetary actions—like those in the fiscal field—must surely be determined by other considerations in addition to their impact upon interest rates and the prices of securities. Again, however, such effects are not to be ignored.

SOME FINDINGS ABOUT MARKET FUNCTIONING

While the study indicated certain broad lessons from the 1957-58 experience for both investors and national financial policy, and also highlighted some of the fundamental and conflicting dilemmas inherent in such a period, it focuses on the functional and mechanical aspects of the Government securities market in this setting of recession and recovery. A specific interest was the speculative and credit excesses that developed. Our objective in studying these developments was to arrive at possible adaptations of public policy and also of market institutions which might lessen the market's exposure to such excesses in the future.

The excesses which occurred last year were associated with the buildup in the Government securities market prior to the Treasury's offering in late May 1958 of 2½ percent, 7-year bond as one option available in its June 15 refinancing of \$9½ billion of maturing obligations held by the public. The other option was a 1-year 1¼ percent certificate. Altogether the holders of about \$7½ billion of the maturing issues preferred the 2½ percent bonds—a figure which was more than double what had been estimated by the financial community or by Government agencies as true investor demand. This was a surprise to the market and suggested that a sizable amount of the newly acquired securities were speculatively held. Nevertheless, there was general market agreement after the announcement was made that the market would be able to absorb the excess supply over a period of time.

About this same time, however, market observers were beginning to realize that the Federal deficit in the year ahead would be the largest since World War II, and that most of it would have to be financed in the second half of 1958, coinciding with the period of heavy Treasury seasonal borrowing. At least part of the flow of economic information in the first half of June had been mildly encouraging; but it was not until around mid-June that market observers took into account that economic recovery might soon begin and that conditions of active ease in credit markets might be coming to an end. In this setting, liquidation of temporary holdings of 2½ percent bonds began and gathered rapid momentum, with an accompanying sharp decline in market prices of Government securities and an associated sharp rise in security yields. As you know, the opportunity for either profits or losses on the price behavior of a longer term bond is much greater than on short-term securities for a given change in interest rates.

This liquidation period, you may recall, occasioned intervention in the market, first by the Treasury in late June and early July to relieve the market of some of the excess supply of 2½ percent bonds issued at mid-June, and second by the Federal Reserve later in July to correct a disorderly condition which developed around the time of the international crisis in the Middle East and a Treasury financing.

Many observers have placed principal blame for this upsetting market episode on excessive speculation in the June refundings, financed by the use of credit extended on unduly thin margins. Our study shows that there was indeed a substantial volume of credit-financed participation in the June refunding—about \$1.2 billion. Considering that \$7½ billion of the 2½ percent bonds were issued, it is obvious that at least four-fifths of the subscriptions represented outright holdings. A significant share of these were probably also temporary holdings purchased in the hope of speculative gain. The outright holdings largely represented subscriptions on the part of commercial banks and business corporations.

In retrospect, one key to this widespread speculation may have been the absence of adequate information about current tendencies in the Government se-

curities market itself, which is, of course, the pivotal market in this economy's financial organization. Much more important, however, is the fact that too many speculatively motivated exchanges into the 2½ percent bonds were apparently based on investor judgments that recession would continue for some time, and that long-term interest yields would decline further.

Speculation financed by credit created a particular problem in this instance because there were large blocks of holdings acquired by newcomers to the market who bought or made commitments to buy Government securities on very thin margin—or in many cases on no margin at all. Several stocks exchange houses made large commitments themselves and acted between lenders and speculators. Some commercial banks and business corporations, actively seeking higher yielding outlets for funds than were provided by Treasury bills and other short-dated securities, directly or indirectly helped to finance these operations.

The activities of one stock exchange member specializing in money brokerage facilitated the financing of a substantial volume of the June rights. These operations were found to be in violation of stock exchange rules. The enforced unwinding of these very large positions came at a particularly sensitive stage of the market decline and, combined with other liquidation of speculative holdings, put the market under severe supply pressure. The New York Stock Exchange has since modified its rules so as to prevent a repetition of this kind of speculative financing activity in the future.

While positions financed on credit were not the largest speculative element in the market at the time of the June refunding, they were certainly important in initiating and accentuating the June–July decline in market prices which accompanied the economic upturn. Once liquidation of the new Treasury bonds was underway and prices were declining sharply, it was inevitable that some margin calls and related selling to protect lenders' positions would occur. At the same time, there was substantial liquidation by holders who had done no borrowing at all as they realized that profits were not in prospect and sought to minimize or avoid losses by selling out. The development of the Lebanon crisis in mid-July and the growing awareness of the prospects of large Treasury deficit financing in a period of rising private demand for loan funds and accompanying expectations of tightening credit conditions, based in part on rumors of a shift in Federal Reserve policy, heightened market uncertainties during this period of liquidation. There also was considerable uneasiness due to fears that the large budgetary deficit would induce renewed inflationary pressures.

Over this entire period of rapid market change, the figures compiled for the study indicate that dealers operated chiefly in their normal primary function as intermediaries. As the June financing approached, dealers were called upon to absorb large amounts of short-term issues that were being sold to meet corporate liquidity needs over dividend dates and the June tax period. As a result, dealers' holdings of Government securities increased substantially. The enlargement occurred mainly in Treasury bills and in June "rights" (maturing issues eligible for the exchange), and these rights were largely exchanged for the 2½ percent bonds.

To make matters more difficult over the period covered by the June financing, dealers had to meet large maturities of repurchase agreements which they had made with nonfinancial business corporations. Under these agreements, corporations accumulating funds in earlier months invested a large portion of them by arrangements to buy Government securities and, at the same time, agreeing to resell the securities to dealers on a fixed date in June—again to cover cash needs related to dividend and income tax disbursements at that time. The short-term securities underlying these arrangements had to be refinanced in June through placement by dealers with banks or other lenders.

When the June exchanges were completed dealers undertook to accomplish a distribution of their underwriting holdings of the new 2½ percent bonds. Such underwriting can result in losses as well as profits to dealers because of the market risks assumed by them. These risks proved to be real in the June financing. Normally, the distribution of the securities acquired in underwriting would have proceeded throughout the remainder of June and July. In view of the then existing market uncertainties, dealers intensified their distribution efforts and cut back on their total positions generally. These activities also contributed to supply pressures in the market.

Once market decline had set in, investors, speculators, and dealers were obliged to make market judgments in the light of their own portfolio and speculative situations and their individual appraisal of current and future uncer-

tainties. There were times in this period, we were told by market participants, when dealers in order to protect their own capital positions would accept large-size orders to sell only on an agency basis, promising to make the best effort possible to carry out the customers' requests. The volume of Government security transactions by the dealer market, however, continued large throughout the decline.

The question still to be answered from our examination of the 1957-58 market experience is just what specific findings and interpretations may be drawn about market excesses and mechanisms. While any specific conclusions at this stage are subject to later modifications or supplement, the following are the main ones drawn by the study group in the preliminary version of part II of the study (ch. VIII).

"(1) Investor and speculator judgments in the late spring period preceding the June refunding were made largely in the light of information pertaining to an economic situation of 1 to 2 months earlier. This lag in the flow of economic information was a factor of basic import in conditioning expectations in this critical period of market development. The role of changing market expectations as to the economic outlook in this period of 1958 clearly emphasizes the need for an adequate supply of current information about trends in the economy generally to facilitate the orderly functioning of financial markets.

"(2) Underlying the late spring speculative positioning of Government securities was a very low absolute level of short-term market interest rates, as well as an unusually wide spread between short- and long-term market yields. This low short-term rate level, together with the prevailing yield structure, vitally influenced the shaping of market expectations of further increases in Government bond prices. It further provided the incentives that led to unusual adaptations of customary credit instruments and terms, which facilitated a rapid swelling in the market's use of credit. This development made the market vulnerable to liquidation pressures.

"(3) These conditions in the market, along with investor expectations of still higher prices of Government bonds, resulted in a situation whereby market participants in the June refunding were encouraged to convert an undue amount of short-term issues into longer term issues, thus oversupplying the longer term area of the market and at the same time sharply reducing the market supply of short-term instruments. Pressure on earnings created by the low level of short-term yields led many banks and some corporations to reach out for the higher yields available in the June financing in an effort to protect their earnings.

"(4) Speculative positioning of 'rights' to the June refunding on the part of outright owners, together with the conversion into 2½ percent bonds of a disproportionate amount of their investment holdings of the maturing issues, was of greater volume than speculative positioning by investors who financed by credit. A large number of banks and business corporations participated in this outright speculative positioning.

"(5) Although speculation on an outright basis in the June financing was larger than credit-financed speculation, the latter was excessive considering the size of the refunding operation. Moreover, liquidation of credit-financed positions appeared almost immediately upon the settlement date for the refunding for various reasons and both triggered and accentuated the declining phase of the market.

"(6) The equity margins put up in this period by credit speculators were, in too many instances, either nonexistent or too thin. Despite the low margins, the losses suffered on credit-financed transactions were incurred chiefly by the borrowers rather than the lenders.

"(7) In the speculative market buildup, the use of the repurchase form of credit financing as a vehicle to carry the speculative positions of nonprofessional and unsophisticated participants proved to be unsound. Use of this particular type of financing instrument, in effect, resulted in lenders advancing credit to unknown borrowers of unknown credit standing or capacity.

"(8) Even among known borrowers of professional standing the use of the repurchase agreement device was stretched in terms of the types of the security which it covered. In the past this instrument was employed in the dealer market mainly to finance securities of the shortest term. In its 1958 market usage the instrument was extended in numerous instances to longer term securities where the maturity bore little or no relationship to the date of termination of the agreement.

"(9) Where used in the mid-1958 period to finance holdings of longer term securities, the repurchase agreement technique in some cases provided a convenient means to circumvent owners' equity requirements that would have been applicable on loans through margins required by lenders.

"(10) The use of forward delivery contracts in the pre-June market buildup involving 'rights' to the June exchange offerings, though of lesser magnitude than repurchase financing, nevertheless facilitated an excessive amount of speculative positioning in this issue without any commitment of purchaser funds.

"(11) In the pre-June market buildup, dealers and brokers were not always aware that their credit standing was in effect used by others to underwrite speculation with no equity. The preponderance of June 'rights' among the forward delivery contracts would suggest a strong preference for 'new' Treasury issues as the mechanism for this speculation.

"(12) The total number of commercial banks outside New York City and also the total number of nonfinancial corporations drawn into the credit financing of the mid-1958 speculative buildup was relatively small, and the major portion of the credit extended was from only a few banks and business corporations.

"(13) In the late spring market buildup some lending by New York City banks, collateralized by Government securities, was at rates and margins that under the prevailing market psychology and the then existing conditions was conducive to the financing of speculative positions.

"(14) The sizable increase in dealer positions prior to the Treasury's June 1958 financing was partly associated with the heavy volume of market trading in that period. Although largely concentrated in short-term securities, the expansion dealer positions did provide a market for these issues which facilitated the lengthening of portfolios and speculative positioning by many investors during the period, particularly banks.

"(15) Even though dealer positions at the time of the June refunding were heaviest in the short-term maturities in the market, liquidation of these positions in the following 3 months, though largely necessary to protect dealer capital positions, did add significantly to the supply pressures otherwise present in the market during this liquidation phase.

"(16) The extensive use of the repurchase instrument for financing all types of Government securities in late spring of 1958 resulted in very large repurchase maturities in mid-June coincident with other churning in the money market in connection with settlement for the Treasury refunding. The necessity of refinancing the securities underlying these repurchase transactions put the Government securities market under heavy internal strain at that time.

"(17) The absence of a Treasury tax anticipation security maturing at mid-June led to much corporate interest in the June maturities as corporations made use of these issues to invest accumulating funds to meet their June tax and dividend needs. This accounted for a considerable part of the market churning at the time of the refunding.

"(18) The availability of regularly issued statistical information about the market itself might have succeeded to some extent in forewarning market participants and interested public agencies of potential speculative dangers around mid-1958. The fact of the matter, however, is that no such objective information was available to either group to gauge the extent of the speculative forces that were present in the market.

"(19) In the closing months of 1958, when many commercial banks were experiencing seasonal credit demands, study data show a movement of funds from the Government securities market to the banks effected through the vehicle of the repurchase agreement. In other words, some dealers were functioning as money brokers, acting as principals in obtaining funds from business corporations under repurchase arrangements and in turn supplying funds to banks under a reverse repurchase arrangement (resale agreement) with them. Question can be raised regarding the appropriateness of a money brokerage function as part of the dealer operation.

"(20) Most of the decline in market interest rates on Government securities, following confirmation in the late fall of 1957 that economic recession had set in, was effected within a short-time span—less than 4 months. The sharp rise in market rates on Treasury issues, following confirmation after mid-1958 that economic recovery had begun, was likewise effected in a short-time span—about 4 months. Although liquidation of Government security positions, built up in hopes of speculative gains in the June refunding, played a central role in accentuating the rise in market interest rates after mid-1958, it does not

necessarily follow that the upward interest rate movement of the entire recovery period would have been smaller if the earlier speculative distortions had been avoided. Upward pressures on interested rates from cyclical Federal deficit financing in combination with expanding private demands for financing, given the savings supply over these months, would still have resulted in a substantial, if not identical, rise in market interest rates."

AN ORGANIZED EXCHANGE OR A DEALER MARKET?

At the hearing of the Joint Economic Committee earlier this year on the President's Economic Report, there was some discussion of the functioning of the Government securities market. The question was raised whether the market might not be more effective if it were a formally organized exchange or auction-type market, with maximum current publicity on transactions rather than an informal over-the-counter dealer market subject to more limited public observation.

As part of this current study of the Government securities market, accordingly, we not only raised this question with market participants but asked our study group to provide a special technical evaluation of the suggestion. The New York Stock Exchange also gave very careful consideration to the question and reported its conclusions to us.

A specialized market tends to develop in a particular form as the individual participants compete to serve more efficiently and economically the needs of buyers and sellers of the kind of security or commodity traded. The present market mechanism for Government securities has grown as a specialized market ever since World War I. Transactions in Treasury issues in the 1920's were carried out both on the New York Stock Exchange and through the over-the-counter dealer market. Even during the early 1920's, however, a steady decline in transactions on the auction market represented by the exchange and a steady rise in the volume handled on dealer markets was taking place. By the mid-1920's, the dealer market was dominant and agency transactions of the Federal Reserve Bank of New York for the account of the Treasury were moved to the dealer market.

Only marketable Treasury bonds are listed on the New York Stock Exchange and this has been true throughout its history. Therefore, the introduction of the Treasury bill in 1929 and its subsequent development as the primary liquidity instrument of the money market—a development accelerated by war and postwar financial trends—further added to the importance of the over-the-counter dealer market. The growth in the Federal debt in the 1930's and during the war years, together with the broader participation of large financial institutions in the market, greatly increase the size of typical market transactions in Governments. Large transactions are more efficiently managed in a dealer-type market, and consequently the number of transactions that could be effectively handled through the auction mechanism of the exchange continued to decline. By 1958 trading in Government bonds on the exchange had dwindled to an insignificant volume in comparison with trading in such securities in the over-the-counter dealer market.

The standards of performance to be applied in evaluating the present dealer market are, of course, related to the specific job which the market has to do as well as to the public interest in a well-functioning market economy. The job to be done first of all is the matching up of purchases and sales by investors and traders. But it also involves the Treasury as issuer of new securities and the Federal Reserve through the execution of its monetary policies. It is the conclusion of our joint study to date that both the broad public interest and the special interests of the Treasury and the Federal Reserve—which are, of course, designed only to serve the public interest—are being effectively served through the present market. Those who participated in our study, including a broad range of investors as well as dealers and brokers, were virtually unanimous in the view that the present type of over-the-counter dealer market in Government securities is preferable to an exchange, auction-type market. Even if confined to bonds, and therefore excluding bills, certificates, and notes, the exchange-type market was regarded as an unsatisfactory alternative.

Probably the most important standard of performance required of the Government securities market in serving existing interests is its ability to handle without disruptive price effects the typically large transactions that arise as large institutional holders adjust their liquidity and investment positions. These individual transactions—by commercial banks in adjusting their reserve and

portfolio positions, by corporations adjusting to their cash flow needs around dividend and tax dates, or by savings institutions or other institutional investors in making portfolio changes—often run to many millions of dollars, particularly in short-term issues. If these holders were unable to purchase and sell readily in such large amounts, their interest in Treasury issues would decline.

The dealers in Government securities appear to have developed better facilities and techniques for handling large transactions promptly and without excessive price effects than would be possible in an organized exchange. They do this by purchasing and selling for their own account; by maintaining substantial inventories of securities in different maturity categories; by a chain of transactions with other dealers—purchases, sales, and exchanges or swaps; and by keeping themselves informed, through their nationwide organizations or correspondent networks, of major sources of supply and demand for Government securities throughout the country. In its operations, the dealer market acts as a buffer to equalize hourly and daily movements in supply and demand, and to absorb the impact of large individual transactions that might otherwise result in abrupt price effects or undue delays in execution of orders.

The specialized dealer market provides a number of other services that institutional customers consider to be valuable. The cost of a transaction in this market is very small because of the large volume of business, because of keen competition among dealers, and because dealer profits do not depend solely on trading margins. A significant part of dealers' earnings is derived from managing their own portfolios and from supplying, through repurchase agreements, investment instruments which have the exact maturity date needed by customers. Such operations also, of course, involve risk of loss.

The dealer market is effectively organized to serve customers throughout the country even though its organization is informal. Transactions are completed promptly by telephone and customers know the price or price range when the order is placed for execution. Moreover, through their intimate experience with the highly technical aspects of each Treasury issue as well as the ways in which the Treasury, the Federal Reserve, and the money market operate generally, dealers provide specialized market advice that customers value. The primary dealers further provide important services in the secondary distribution of new Treasury issues. They also provide a convenient point of contact for Federal Reserve open market operations in short-term Government securities.

The major defects attributed by some critics to the dealer market in U.S. Government securities reflect three features: First, the market is concentrated in a relatively small group of primary dealers, and therefore may not be as competitive as an organized exchange market; second, there is little information about its operations, without supervision or formal rules governing its practices, despite its special public interest; and third, the market is not geared to handling small and odd lot transactions nor is it especially interested in them.

As to competition, there is no question that the primary dealer market is very highly competitive, even though it comprises only 12 nonbank firms and 5 bank dealers, most of whom have central offices in New York City. There is necessarily spirited competition between the dealers for the available volume of trading business. Any offers to sell at a price even slightly below the market usually are quickly taken advantage of, as are offers to buy at anything above whatever the price may be at the moment. In volume, the Government securities market is by far the largest financial market in the country. It handles each year a dollar volume of transactions approximating \$200 billion, or more than 3 times as much as the dollar volume of transactions in all corporate stocks as well as bonds on the New York Stock Exchange.

The dealers are principally wholesalers and their customers consist of several hundred nonfinancial corporations, several thousand commercial banks who submit orders both for their own account and for customers, other security brokers and dealers handling transactions for customers, hundreds of insurance companies, mutual savings banks, pension funds, and savings and loan associations throughout the country, the special funds of State and local governments, personal trust accounts, and some individual investors of substantial means. These investors and traders who use the market to buy or sell are generally themselves expertly informed and experienced in investment matters. Each is seeking the best return on the funds he places in Government securities; each is continuously comparing these returns with those on alternative investment opportunities; and each of the larger investors, who regularly use the services of several dealers, is constantly comparing the relative performance of the dealers with whom he is in contact.

In this type of highly competitive market, the dealer who succeeds must execute the buy or sell orders of these numerous and varied investors promptly and efficiently and the business must be handled in accordance with high ethical standards. Moreover, if he is to obtain future business, such investment advisory services as the dealer renders his customers must stand the test of time.

Each of the primary dealers, through one means or another, operates throughout the country because broad coverage is essential to the maintenance of a sufficient volume of business for profitable operations. This is probably a major reason why there are not more dealer firms active in the market. Another reason, according to information received in this study, is that the number of qualified and experienced personnel available to staff new firms is relatively small.

Regarding the criticism of market mechanics, it is true that the dealer market makes available to the public practically no information on its operations other than market bid and offer quotations. There is no requirement for making available either to the public or to a duly constituted authority the records of dealer net positions in securities or amounts borrowed, such as are required of members of the New York Stock Exchange.

The lack of formal rules, supervision, and adequate information leaves the market open on occasion to suspicion that it may not always be operating in the public interest. It has been suggested that in instances dealers' interests may conflict with those of customers, that dealer operations may unduly accentuate swings in securities prices, and that dealer advice may not be entirely accurate. There was, however, little or no evidence gathered in the study that such problems are common in the dealer market. All of the market customers consulted in the present study expressed their full confidence in the Government securities dealers, individually and as a group, and testified to their high standards of integrity and business practice.

Concerning small transactions in the market, consultants to the study have indicated that they generally go through other brokers and dealers and commercial banks, and that when they reach the market they are handled promptly by dealers at a relatively low cost that is in part subsidized by the large transaction. As the dealers are organized primarily to handle large transactions, it is understandable that they view the small deals as an accommodation, and do not actively encourage them. It seems clear that if facilities designed more specifically to serve small investors' interests in marketable bonds are to be established, there would have to be some additional incentive provided.

The New York Stock Exchange, prompted by our study, reviewed the potentialities for reestablishing a vigorous auction-type market in Government securities on the exchange. After extended consideration of the matter, however, exchange officials concluded that, even though such a development was theoretically possible, problems raised by the suggestion would be insurmountable unless both the Government and the exchange shifted a number of fundamental policies.

One specific problem to be resolved is the difficulty under existing conditions of encouraging exchange specialists to take the financial risk of making a market in Government securities. The specialists would be in competition with established Government securities dealers. In addition, they might on many occasions need to build up very large positions in Government securities, since this is a heavy volume market and, when sharp price movements occur, quotations on maturities throughout the list tend to move together much more so than in the market for specific corporate stocks or bonds. Finally, because of the public nature of transactions at exchange trading posts, specialists taking positions to make orderly and continuous markets would be unduly exposed to possible raids by nonmember dealers and other large traders.

There is also the problem of developing an adequate incentive for handling Government securities on the exchange through a commission schedule that would be competitive with narrow spreads prevailing in the dealer market.

Other conditions set by the exchange for an effective auction market under its auspices would be—

- (a) A larger supply of long-term Government bonds in the market, especially of bonds attractive to individual investors through tax exemption or other special features since these investors now find only limited interest in Governments other than savings bonds.

(b) The placing on the exchange of all Federal Reserve agency transactions in bonds, possibly plus official support of the exchange market; and

(c) A potential requirement for the execution of all transactions of member firms in Government bonds on the exchange, except for some off-flavor trades in special circumstances.

(d) Some protection of the position of member firms who are acting as Government security dealers.

The exchange did not suggest that its facilities could be adaptable at all to trading in Treasury bills, certificates of indebtedness, or notes, which together constitute more than half of the outstanding marketable Federal debt and are also the issues in which the overwhelming volume of market transactions takes place.

These conditions make it clear to us that it would be difficult to develop an auction-type market for Government securities on a broad scale under the existing organized exchange mechanism.

The alternative approach of improving the mechanism and institutions of the present Government securities market, by carefully studying and remedying defects in the dealer market as they come to light, appears to us to promise results that will serve the public interest. At the same time, the New York Stock Exchange should be encouraged to develop further the auction facilities it now provides for transactions in Government bonds. The total market cannot be harmed, and may indeed be improved by more active competition between the exchange market and the dealer market in bond trading.

AREAS FOR IMPROVING MARKET MECHANISMS AND FUNCTIONING

Our study was launched, as stated earlier, in the hope that the suggestions advanced and problems revealed might indicate certain improvements in the way the Government securities market operates, with particular emphasis on the prevention of future speculative excesses in the market. In the light of consultants' suggestions and of findings of our factual review of the 1957-58 market experience, our study group initiated four supplementary studies to evaluate possible means of improving the market's functioning. These are in the nature of working papers for consideration by Treasury and Federal Reserve officials. As their preparation has just been completed in preliminary form, they have not yet been reviewed. Hence, they cannot be interpreted as reflecting any official recommendations for market improvement. There may also be other supplementary studies undertaken as we reexamine market processes and mechanisms and we naturally intend to pursue this phase of our inquiry as far as will serve a constructive purpose.

A first area of supplementary study pertains to the adequacy of statistical and other information relating to the dealer market. As mentioned earlier, it is commonly recognized that openly competitive and efficient markets are characterized by informed buyers and sellers. A broad range of objective information needs to be available to serve effectively the interests of all market participants, including the Treasury as issuer of securities for the market and the Federal Reserve as it participates in the market in regulating overall credit and monetary conditions. In this light the present flow of information relating to the market is inadequate, a point that was agreed to by many of our study consultants.

As a result, our study group undertook a thorough analysis of the information that ought to be regularly available. We were encouraged in this by the excellent cooperation received from dealers and other market participants in supplying information for our review of market experience in 1957-58. We believe, therefore, that a reporting program can be worked out by the Federal Reserve and Treasury staffs to put an adequate information program into active operation in the not too distant future.

A second area of supplementary study is the credit financing of Government securities transactions. Last year's market experience has clearly indicated that at times an undue amount of speculation financed on thinly margined credit can be detrimental to the market and that competition of lenders in extending credit to prospective holders may result in deterioration in appropriate equity margin standards. This experience raises the question of the need for some action to assure that sound credit standards will be consistently maintained by lenders in credit extension backed by Government securities and also to keep the total volume of such credit from expanding unduly at times.

Our study has indicated that there are three approaches which the Government might consider in dealing with this problem: first, a statement by bank supervisors to each lending institution within its jurisdiction indicating minimum margins to be adhered to as standard; second, a requirement that each investor participating in the exchange of maturing Treasury issues for new issues state his equity position in those securities in compliance with Treasury standards (plus the continuing requirement by the Treasury of appropriate deposits on subscription to its new issues offered for cash); and, third, the introduction of special margin regulation, similar to that now applicable under the Federal Reserve Board regulations T and U to the purchasing or carrying of corporate securities. The latter type of regulation would, of course, require congressional action, since present law specifically exempts Government securities from this type of credit regulation. It must be reemphasized here that these are merely possible approaches; they have not yet been fully appraised by either Treasury or Federal Reserve officials and other alternatives may be developed in the light of additional study.

A third area for special study is the use of the repurchase arrangement in credit financing of Government securities. This is not a new method of credit financing, but it is a method that is easy to apply to Government securities transactions and, because of its flexibility and adaptability, has become much more popular in recent years. Government securities market activity last year brought to light certain uses of repurchases that were not in the public interest when such financing was arranged without the borrower putting up adequate margin. The study discusses various alternatives which might be applied to prevent future abuse.

A fourth area of special study of the existing mechanism of the Government securities market relates to its present lack of formal organization. In our consultations, a number of market participants and observers suggested that the market might be improved and strengthened through cooperative action of primary dealers themselves, working through a dealers' association. Various specific functions that an association might perform to improve the market's functioning were indicated, including: (a) the adoption of standard rules to assure fair treatment of buyers and sellers in both large and small transactions; (b) the development of standard practices to help maintain dealer solvency; and (c) greater liaison between the Treasury and the dealers in Treasury financing operations. It was also suggested that a dealers' association could be useful in identifying primary dealers in Government securities both to improve dealer service and to apply any market rules which may be adjudged in the public interest. Since the possible advantages of such an organization as well as its possible disadvantages obviously require careful and detailed examination, the task of this supplementary study has been to make this much-needed evaluation.

A question that naturally arises at this point is whether in the light of the present study there will be any occasion later for special legislative requests pertaining to the operation of the Government securities market. This question cannot be answered yet. Before it is, we must try to determine what can be accomplished in improving market processes and mechanisms without legislative action and then ask whether these improvements are enough. The fact of the study itself, together with educational efforts undertaken by the Treasury and Federal Reserve System, has already set in process a fuller appreciation on the part of market participants of the undesirable effects of certain market practices. If we find that desired improvement of market mechanisms and institutions requires new statutory authority, we will propose appropriate legislation to the Congress.

Markets are dynamic economic institutions. They require successive adaptation to changing needs. From the standpoint of the public interest, study of these adaptations is never ending. Study efforts may be intensified from time to time as the case of the present Treasury-Federal Reserve study, but they are basically continuous. Continuing observation and study of the Government securities market is a responsibility which both the Treasury and the Federal Reserve recognize.

In conclusion, we repeat that improvement in the processes and mechanisms of the Government securities market will in no way solve our problems of fiscal imbalance. Nor can they correct our problems of too much short-term public debt; of our need for continuous flexibility in our approach to monetary policies; of attaining a volume of savings which will match our expanding investment needs; or of the cyclical instability of our financial markets. These are basic

problems. We must all work toward their ultimate solution in the public interest.

Representative PATMAN. Thank you very kindly, sir. We appreciate your making yourself available.

Secretary ANDERSON. Thank you, Mr. Chairman.

Representative PATMAN. If you will answer those question for the record, we will appreciate it.

Secretary ANDERSON. Yes; we will do that.

(At the request of the chairman, the following is made a part of the record:)

The following is an excerpt from hearings before a subcommittee of the Committee on Government Operations of the House of Representatives on Debt Management Advisory Committees, Treasury Department, held June 5 and 7, 1956:

Date of committee report	Financing problem	Committee recommendations	Treasury offerings
1952 Feb. 8.....	Refunding of 2½-percent bonds maturing Mar. 15, 1952.	Offer exchange for notes or bonds with maturity of 3 to 6 years and coupon of 2¼ to 2¾ percent, depending on maturity.	Offered exchange for 2¾-percent bonds due Mar. 15, 1959.
	Refunding of 1¾-percent certificates maturing Apr. 1, 1952.	Offer optional exchange for 1¾ percent, 11½- or 12-month certificates or the same notes or bonds suggested above.	Offered single exchange for 1¾-percent 11-month certificates.
	Call of 2- and 2¼-percent bonds eligible for redemption.	Do not make call at this time.	Call was not made.
	Cash offering of long-term bonds.	Offer \$1 billion on Mar. 15 or Apr. 1 of 35-year 3-percent bonds.	No long-term bonds issued.
Apr. 4.....	Cash required to cover deficit of upward of \$10 billion.	Offer long-term marketable 3-percent bond with maturity of 30 years. Market should be approached experimentally with initial offering of \$1 billion to \$1½ billion.	Marketable bond not offered. Reopened 2¾-percent nonmarketable bonds due 1980 in May for cash and exchange for outstanding marketable 2½-percent bonds.
		For short-term borrowing, increase offerings of bills.	Weekly issues of bills were increased by an aggregate of \$1.6 billion between Apr. 7 and July 3.
		Revise savings bond program: Increase yield on series E to 3 percent; offer new 3 percent current-income bond as companion to series E bonds; adopt more favorable yield curve modified to yield 2¾ percent for 12 years on series F and G bonds.	Savings bond program was revised on May 1 along the basic lines recommended by committee.
	Refunding of short-term bills and certificates.	Treasury should feel its way as year goes on, and roll over maturities into similar issues or wherever possible, into medium-term issues.	All maturities were rolled over.
	Call of 2- and 2¼-percent bonds eligible for redemption.	Under present conditions issues should not be called.	Call was not made.
June 27.....	Refunding of certificates due Aug. 15 and Sept. 1, 1952.	Suggested combined refunding into a similar certificate or note.	Offered exchange for 2-percent certificates due Aug. 15, 1953.
	Refunding of 1¾-percent certificates due Oct. 1, 1952.	Roll over into similar obligation.	Offered 2½-percent 14-month note due Dec. 1, 1953.
	New cash of \$5 billion in second half of year.	Issue long-term marketable bonds at appropriate rate in autumn; revise rates on tax notes; issue tax bills maturing around the March tax date; sell larger amounts of 90-day bills.	No long-term bonds issued. Sold in October \$2.5 billion tax-anticipation bills due Mar. 18, 1953; also in November \$2 billion tax anticipation bills due June 19, 1953.
	Call by Aug. 15 of 2- and 2¼-percent bonds eligible for redemption on Dec. 15, 1952.	Do not call under present circumstances.	Call was not made.

Date of committee report	Financing problem	Committee recommendations	Treasury offerings
Dec. 5, 1952	<p>Refunding of 1½-percent certificates due Feb. 15, 1953.</p> <p>Call of 2- and 2½-percent bonds eligible for redemption.</p> <p>Handling maturity of series F and G bonds.</p> <p>Cash offering of long-term bonds in first half of 1953.</p>	<p>Optional exchange for a certificate or note due in about 1 year at an appropriate rate, or a bond maturing in 1956, 1957, or 1959.</p> <p>Call partially tax exempt 2-percent bonds of June 1953-55. Do not call fully taxable 2½-percent bonds.</p> <p>Secure broad permissive legislation to extend series F and G bonds at maturity.</p> <p>Extension of maturities can be determined from time to time only in light of investment market; sound out market for long-term bond as conditions appear propitious.</p>	<p>Offered optional exchange for 2¼-percent 1-year certificates or 2½-percent 5-year 10-month bonds due Dec. 15, 1953</p> <p>Call of 2-percent bonds was made.</p> <p>Call of 2½-percent bonds was not made.</p> <p>Series F and G bonds were not extended.</p> <p>(See meeting of War. 20, 1953.)</p>
Mar. 20, 1953	<p>Refunding of 1½-percent certificates due June 1, 1953, and 2-percent bonds recalled for redemption on June 15, 1953.</p> <p>Cash offering to cover attrition on refunding and apparent cash deficit.</p>	<p>Offer optional exchange for either 1-year 2¼-percent certificates or a short-term bond, due around 1961.</p> <p>Time was not opportune for sale of long-term bond and no cash offering should be made in May or June. Suggested consideration of the short-term bond due around 1961.</p>	<p>Offered single issue of 2½-percent certificates due June 1, 1954.</p> <p>Offered for cash subscription \$1 billion of 3¼-percent bonds, dated May 1, 1953, and maturing June 15, 1953.</p>
	<p>Refunding maturing series F and G bonds.</p>	<p>Offer holders in exchange a 3-percent marketable bond maturing in 7½ years to test the market for a moderately long-term bond.</p>	<p>Exchange offer was made for 3¼-percent bonds maturing June 15, 1953.</p>
June 19	<p>New cash of \$5 billion in July.</p>	<p>Offer tax anticipation certificates maturing Mar. 15, 1954, at rate determined by market conditions which would prevail in July.</p>	<p>Sold for cash \$5.9 billion 2½-percent tax anticipation certificates due Mar. 22, 1954.</p>
	<p>Refunding of 2-percent certificates on Aug. 15, 1953.</p>	<p>Refund with 1-year certificates, or possibly a somewhat longer issue if conditions at time favor it.</p>	<p>Offered exchange for 1-year 2½-percent certificates.</p>
Aug. 26	<p>Refunding of 2-percent bonds maturing Sept. 15, 1953.</p> <p>New cash of about \$2.5 billion in October.</p>	<p>Offer optional exchange for 1-year 2½-percent certificates or 2½-percent notes maturing in about 3½ years.</p> <p>Preliminary recommendation to sell additional notes of about 3½-year maturity, or longer if market conditions are favorable. Would not be prudent to sell new long-term bonds at this time.</p>	<p>Offered optional exchange into 1-year 2½-percent certificates or 3½-year 2½-percent notes.</p> <p>(See meeting of Oct. 13, 1953, below.)</p>
Oct. 13	<p>New cash of \$1½ to \$2 billion in early November.</p> <p>Refunding of 2½-percent notes on Dec. 1, 1953.</p>	<p>Issue \$2 billion of 2¼-percent bonds maturing in 3½ to 6 years.</p> <p>Preliminary recommendation for offer of an optional exchange for short-term and intermediate-term bonds (12- to 14-year 3-percent bond, or longer if market conditions permit). Exact terms would have to be determined by prevailing conditions at time of offering.</p>	<p>Offered late in October \$2.2 billion of 2¼-percent bonds maturing Sept. 15, 1961.</p> <p>(See meeting of Nov. 13, 1953, below.)</p>
Nov. 13	<p>Refunding of 2½-percent notes on Dec. 1, 1953.</p>	<p>Offer optional exchange for 2-percent notes maturing Mar. 15, 1955, or 3-percent bonds of about 15-year maturity; however, if holders of series F and G bonds maturing in 1st half of 1954 are not also offered the right to exchange into the same 3-percent bonds, the longer part of the optional exchange should be 2½-percent bonds maturing Dec. 15, 1958.</p>	<p>Offered optional exchange of 1½-percent notes maturing Dec. 15, 1954, or 2½-percent bonds maturing Dec. 15, 1958.</p>

Date of committee report	Financing problem	Committee recommendations	Treasury offerings
1953 Nov. 13.....	Refunding 2¼-percent certificates on Feb. 15, 1954, and 1½-percent notes on Mar. 15, 1954.	Consolidate issues in single refunding operation. Specific recommendations could not be presented at this time.	(See meeting of Jan. 20 1954, below.)
1954 Jan. 20.....	Refunding of 2¼-percent certificates of Feb. 15, 1954, and 1½-percent notes of Mar. 15, 1954. Call on Feb. 15, 1954, for redemption on June 15 of the 2¼-percent bonds of 1954-56 and 2¼-percent bonds of 1952-55.	Combine refunding on Feb. 15, 1954, with option to exchange for 13-month 1½-percent notes or 2½-percent bonds maturing in 6½ years or slightly longer. Call should be made for redemption on June 15.	Offered optional exchange of maturing issues for 12-month 1½-percent certificates or 2½-percent bonds maturing in 7 years 9 months. Call was made on Feb. 15, but redemption of these issues, as well as the 2-percent bonds due June 15, was anticipated by offering holders right to exchange on Feb. 15 for the 2½-percent bonds maturing in 7 years 9 months also offered on the refunding.
Apr. 23.....	New cash of \$2 billion to \$3 billion after Mar. 15, 1954. Refunding of 2½-percent certificates due June 1, 1954. Refunding on June 15, 1954, of 2-percent bonds and remaining 2¼-percent called bonds that were not exchanged in February. New cash of \$2 billion in May. Refunding of 2-percent bonds maturing or callable in December 1954.	Sale of 3-percent long-term bonds, maturity to depend upon market conditions at time of offering. Offer holders option of a short obligation maturing within 18 months or 2¼-percent bonds maturing in last half 1960. Offer an exchange into only the short obligation maturing within 18 months. Sale for cash of \$2 billion of 2¼-percent bonds maturing in last half of 1960. Maturity should be anticipated by giving holders the privilege of exchanging into the 2¼-percent bond maturing in 1960. (Committee recommended that all of the above financing be combined in 1 operation in May.)	Offered \$1.5 billion of tax anticipation bills due June 24, 1954. Offered optional exchange for 1-year 1½-percent certificates or 1½-percent notes due Feb. 15, 1959. Offered exchange into 1-year 1½-percent certificates. Offered \$2 billion of 1½-percent notes due Feb. 15, 1959. December maturities were not included in this financing operation. (Financing was combined in 1 operation in May.)
July 9.....	New cash of \$4 billion by Aug. 1, 1954. Refunding of 2½-percent certificates due Aug. 15 and Sept. 15, 1954. Call on Aug. 15, 1954, for redemption on Dec. 15 the 2-percent bonds of 1951-55.	Majority of committee recommended \$2 billion each of 1-percent notes maturing Sept. 15, 1955, and 1½-percent notes maturing Sept. 15, 1957; minority favored tax-anticipation certificates or notes maturing Mar. 18, 1955. Refund together their optional exchange for 1-percent certificates maturing Sept. 15, 1955, or 2½-percent bonds maturing Sept. 15, 1960. Call should be made on Aug. 15.	Sold \$3.7 billion 1-percent tax anticipation certificates maturing on Mar. 22, 1955. Offered optional exchange into 1-year 1½-percent certificates or 2½-percent bonds due Nov. 15, 1960. Call was made.
Sept. 17.....	New cash of about \$3.5 billion in October. New cash of about \$1.5 billion in December. Refunding of 1½-percent notes and 2-percent bonds on Dec. 15, 1954.	Dual offering of 1½ percent tax certificates maturing June 22, 1955, and 1-year certificates of indebtedness. Preliminary recommendation that 3-percent long-term bonds be offered, maturity to be determined by market conditions. Preliminary recommendation that holders be offered an optional exchange of 1-year certificates or medium-term obligations with a maturity not to exceed 10 years.	Sold \$4.1 billion of 1½-percent notes maturing May 15, 1957. (See meeting of Nov. 18, 1954 below.) Do.

Date of committee report	Financing problem	Committee recommendations	Treasury offerings
1954 Nov. 18.....	Refunding of 1½-percent notes and 2-percent bonds on Dec. 15, 1954.	Offer holders option of a short obligation—either 1-year 1¼-percent certificates or 1½-percent certificates maturing Aug. 15, 1955; or a longer obligation—2½-percent bonds maturing in about 8 years.	Offered optional exchange into either: 1-year 1¼-percent certificates or 1½-percent certificates maturing Aug. 15, 1955; or 2½-percent bonds maturing in 8 years 8 months.
	New cash in December....	December cash financing anticipated in September proved unnecessary. Therefore committee recommended that long-term bond should not be offered at that time but should be done on the first appropriate occasion.	No new bond financing was undertaken.
	Issuance of FNMA debentures.	Expressed view that Treasury could sell at least \$500 million FNMA debentures if conditions were set forth as to FNMA credit from the Treasury, restrictions on amount offered against portfolio, maturity, and rate, and fiscal arrangements.	Offered \$500 million of 2½-percent FNMA 3-year notes in January 1955.
1955 Jan. 27.....	Refunding of 1½-percent certificates due Feb. 15, 1955, and 1¼-percent notes due Mar. 15, 1955. Refunding of 2½-percent bonds called for redemption on Mar. 15, 1955.	Offer optional exchange of 1½-percent 13-month notes or 2½-percent notes maturing Dec. 15, 1957. Majority favored optional exchange for 1½-percent 13-month notes or 3-percent 40-year bonds. Minority favored \$1.5 billion cash offering of 3-percent 40-year bonds, with the 2½-percent bonds receiving same exchange option indicated above for the maturing notes and certificates.	Offered optional exchange of 1½-percent 13-month notes or 2-percent notes maturing Aug. 15, 1957. Offered optional exchange of 1½-percent 13-month notes or 3-percent 40-year bonds.
Apr. 17.....	Refunding of 1½-percent certificates due May 17, 1955.	Offer optional exchange for 1½-percent 1-year certificates or 2½-percent bonds due Dec. 15, 1958.	Offered exchange for only 2-percent 15-month notes.
	New cash of \$2.5 billion to cover maturity of tax-savings notes in May and June.	Make cash offering of \$2.5 billion of 1½-percent 1-year certificates.	Offered \$2.5 billion of 2-percent 15-month notes for cash.
		(Committee recommended that the refunding and cash offering be combined in one operation.)	(Financing was combined in 1 operation.)
June 24.....	New cash of \$3 billion in July.	Reopen subscriptions to 3-percent 40-year bonds due in 1955 for cash of \$750 million to \$1 billion; obtain balance through sale of 1½-percent tax anticipation certificates due Mar. 22, 1956.	Offered \$750 million of 3-percent bonds of 1955 and \$2 billion of tax-anticipation certificates due Mar. 22, 1956.
	Refunding of 1½-percent certificates due Aug. 15, 1955.	Offer optional exchange for 1-year 2-percent certificates (or 11-month certificates), or the outstanding 2½-percent bonds maturing Dec. 15, 1958. (Suggested refunding be done at time of cash offering.)	Offered optional exchange for 1-year 2-percent notes due Aug. 15, 1956, or 2-percent tax-anticipation certificates due June 22, 1956. Did not offer the longer option. (Terms of financing were withheld until payment date of cash tax certificate financing announced earlier.)
	Retirement of maturing tax savings notes.	Obtain funds by increasing bill offerings by at least \$100 million each week for cycle of 13 weeks.	Offered \$100 million of additional bills each week between July 27 and Sept. 29.
Sept. 25.....	New cash of \$2.5 billion at end of September.	Offer 2¼-percent tax-anticipation certificates due June 22, 1956.	Sold \$3 billion of 2¼-percent tax-anticipation certificates due June 22, 1956.

Date of committee report	Financing problem	Committee recommendations	Treasury offerings
1955 Nov. 18.....	Refunding of 1¼-percent certificates and 1¼-percent notes on Dec. 15, 1955. New cash of \$1 billion by year end.	Offer single exchange for 1-year 2½-percent certificates. Make cash offering of tax-anticipation bills due Mar. 22, 1956.	Offered optional exchange of 1-year 2½-percent certificates or 2½-year 2½-percent notes. Sold in December \$1.5 billion of tax anticipation bills due Mar. 23, 1956, on competitive bids.
1956 Feb. 29.....	Refunding of 1½-percent notes due Mar. 15, 1956, and 1½-percent notes due Apr. 1, 1956. Call by May 15, 1956, of 2¾-percent bonds of 1956-59 for payment on Sept. 15, 1956.	Suggested combined refunding. Majority favored optional exchange for 2½-percent certificates due Feb. 15, 1957, or outstanding 2½-percent notes due June 15, 1958; also later offering of \$500 million additional 3-percent bonds of 1955 for cash or advance exchange of 2½-percent bonds of 1956-58. Minority favored single exchange for 2½-percent certificates due Feb. 15, 1957, to be coupled with \$500 million cash offering of 3-percent bonds of 1955 at time of refunding. Call should be made.....	Offered optional exchange for 2½-percent certificates due Feb. 15, 1957, or 2½-percent notes due June 15, 1958. No long-term bonds were offered. Call was made.

(The following is the material requested of the American Bankers Association:)

THE AMERICAN BANKERS ASSOCIATION,
New York, N.Y., July 27, 1959.

Mr. JAMES W. KNOWLES,
Economist, Joint Economic Committee,
New Senate Office Building, Washington, D.C.

DEAR MR. KNOWLES: In accordance with your request, I am enclosing three copies of a summary of meetings of the Committee on Government Borrowing covering the period since February 1956 and showing:

- (1) The financing problem.
- (2) The committee recommendations; and
- (3) The Treasury offerings.

Also enclosed are copies of the current membership list of the committee.
Sincerely yours,

EUGENE C. ZORN, Jr.
Secretary, Committee on Government Borrowing.

Date of committee report	Financing problem	Committee recommendations	Treasury offerings
July 12..... <i>1956</i>	Refunding of 2 percent notes due Aug. 15, 1956. Refunding of 2½ percent bonds called for redemption on Sept. 15, 1956. New cash of \$2½ billion in August or September.	Offer exchange for 2½ percent notes due Aug. 1, 1957. Obtain funds by increasing bill offerings by \$100 million weekly for a 13-week cycle. Offer tax anticipation issue due on or about Mar. 22, 1957.	Offered exchange for 2½ percent notes due Aug. 1, 1957. Paid off the bonds in cash. Did not increase weekly bill offering. Sold in August \$3.2 billion of 2½ percent tax anticipation certificates due Mar. 22, 1957.
Nov. 15.....	Refunding of 2½ percent certificates due Dec. 1, 1956.	Offer optional exchange for 3¼ percent tax anticipation certificates due June 21 or 24, 1957, or 3½ percent certificates due Nov. 29, 1957.	Offered optional exchange for 3¼ percent tax anticipation certificates due June 24, 1957, for 3½ percent certificates due October 1, 1957.
Jan. 31..... <i>1967</i>	Refunding of special bills due Feb. 15, 1957, 2½ percent certificates due Feb. 15, 1957, 2½ percent notes due Mar. 15, 1957, and 1½ percent notes due Apr. 1, 1957.	Offer holders of all 4 issues optional exchange for 3½ percent certificates due Feb. 14, 1958, or 3½ percent notes due Feb. 15, 1960.	Refunded bills with tax anticipation bills due June 24, 1957. Offered 2½ percent certificates and 2½ percent notes optional exchange for 3½ percent certificates due Feb. 14, 1958, or 3½ percent notes due May 15, 1960. Offered 1½ percent notes exchange for the 3½ percent notes due Feb. 14, 1958.
Mar. 13.....	New cash of about \$3 billion after March tax date.	Sale for cash of 3½ percent notes due Apr. 15, 1958 with privilege of conversion at maturity into bonds of 12- to 14-year maturity.	Offered \$2½ billion of 3½ percent certificates due Feb. 14, 1958, and \$½ billion 3½ percent notes due May 15, 1960. (This was a reopening of issues offered in February refunding.)
Apr. 14.....	Refunding of 1½ percent notes due May 15, 1957.	Offer optional exchange for (1) certificates due May 1, 1958 at rate of not more than 3½ percent (or a shorter maturity if market rates so dictated) or (2) 3½ percent notes due May 1, 1960 and convertible into 3½ percent 15-year bonds.	Offered optional exchange for 3½ percent certificates due Apr. 15, 1958, or 3½ percent notes due Feb. 15, 1962.
July 17.....	Refunding of 2½ percent notes due Aug. 1, 1957, 2 percent notes due Aug. 15, 1957, 3¼ percent certificates due Oct. 1, 1957, and 1½ percent notes due Oct. 1, 1957.	Offer holders of all four issues optional exchange for 3½ percent certificates due Apr. 15, 1958, or 4 percent notes due in July 1959, with right of holder to extent maturity for 3 additional years.	Offered optional exchange for 3½ percent certificates due Dec. 1, 1957, 4 percent certificates due Aug. 1, 1958, or 4 percent notes due Aug. 1, 1961, but redeemable at option of holder on 3 months' advance notice on Aug. 1, 1959. However, October maturities were restricted to 4 percent certificates or extendable notes.
Sept. 10.....	New cash of about \$3.5 billion in late September and early October. To keep within debt ceiling, \$3 billion before Oct. 1, and the other \$0.5 billion after maturity of Oct. 1 issues.	To obtain \$3 billion, offer \$1 billion of 4 percent certificates due Aug. 1, 1958, and \$2 billion of 4 percent notes due Aug. 1, 1961, redeemable on Aug. 1, 1959 at holder's option. To obtain \$0.5 billion, concurrent with above offering announce offering of 10-year 4 percent bonds, payment to be made in early October.	Offered \$3 billion for cash as follows: \$500 million of 4 percent bonds due Oct. 1, 1960, \$1.75 billion of 4 percent notes due Aug. 1, 1962, but redeemable at option of holder at end of 2½ years, and \$750 million of 4 percent certificates due Aug. 1, 1958.
Nov. 14.....	Refunding of 3½ percent certificates due Dec. 1, 1957. New cash of about \$1.5 billion.	Offer exchange for 3½ percent certificates due Dec. 1, 1958. Offer \$1 billion of 4 percent 5-year notes and \$500 million 4 percent 17-year bonds. Because of debt limit, payment on two issues to be 50 percent on Nov. 26, and 50 percent on or about Dec. 2. If 17-year bond not offered, all \$1.5 billion should be in a 5-year note.	(See meeting of Nov. 18, 1957, below.) See meeting of Nov. 18, 1957, below.)

Date of committee report	Financing problem	Committee recommendations	Treasury offerings
<p>1967 Nov. 18.....</p>	<p>Review recommendations of Nov. 14, 1967, due to change in market following lowering of discount rate.</p>	<p>Offer exchange for 3¼ percent certificates due Dec. 1, 1968.</p> <p>New cash offering of \$1 billion of 3¼ percent 5-year notes and \$500 million of 3¼ percent 17-year bonds.</p>	<p>Offered for exchange 3¼ percent 1-year certificates due Dec. 1, 1968.</p> <p>Offered for cash \$1 billion 3¼ percent notes due Nov. 15, 1962, and \$500 million 3¼ percent bonds due Nov. 15, 1974.</p>
<p>1958 an. 28.....</p>	<p>Refunding: recommend which issues of notes, certificates, and bonds maturing in first half of 1958 should be refunded in early February; whether special bills maturing Apr. 15 should be offered an exchange; and refunding terms.</p> <p>Cash: should offering be made at time of refunding, if legislations raising debt limit passed by then?</p> <p>Call on Feb. 14, 1958, for redemption on June 15, the 2¼-percent tax exempt bonds of 1958-63.</p>	<p>Offer holders of 3½-percent certificates due Feb. 14, 1958, 2½-percent bonds due Mar. 15, 1958, 1½-percent exchange notes due Apr. 1, 1958, 3¼-percent certificates due Apr. 15, 1958, and special bills due Apr. 15, 1958, an optional exchange for 2½-percent 1-year certificates, 3-percent obligations maturing in 5 or 6 years, or 3 ½-percent 30-year bonds.</p> <p>Defer refunding of June maturities.</p> <p>Delay consideration of cash financing until after the refunding and change in the debt limit.</p> <p>Call should be made.....</p>	<p>Offered recommended issues optional exchange for 2½-percent certificates due Feb. 14, 1959, 3-percent bonds due Feb. 15, 1964, or 3½-percent bonds due Feb. 15, 1990.</p> <p>Following refunding operation and raising of debt limit, offered for cash \$1.25 billion 3-percent bonds due Aug. 15, 1966.</p> <p>Call was made.</p>
<p>Apr. 1.....</p>	<p>New cash of about \$3,500,000,000.</p>	<p>Offer \$3,500,000,000 of 2½-percent notes due Feb. 15, 1963.</p>	<p>Offered \$3,500,000,000 of 2½-percent notes due Feb. 15, 1963.</p>
<p>May 29.....</p>	<p>Refunding of 2¼-percent notes, 2¼-percent bonds, and 2¾-percent bonds on June 15, 1958.</p>	<p>Offer holders optional exchange for 1½-percent notes due Aug. 14, 1959, 2½-percent bonds due Feb. 15, 1965, 3-percent bonds due May 16, 1971, or 3¼-percent bonds due May 15, 1985.</p>	<p>Offered optional exchange for 1½-percent certificates due May 15, 1959, or 2½-percent bonds due Feb. 15, 1965.</p> <p>Offered for cash \$1,000,000,000 of 3¼-percent bonds due May 15, 1985, at price of 100½.</p> <p>Refunding limited to June maturities.</p>
<p>July 17.....</p>	<p>Inclusion of two bond issues called for redemption on Sept. 15, 1958, in June refunding.</p> <p>Refunding of 4-percent certificates due Aug. 1, 1958, and bond issues called for redemption Sept. 15, 1958.</p> <p>Cash financing of undetermined amount in August.</p>	<p>Refunding of called bonds should be deferred.</p> <p>Offer holders of all issues exchange for 1½-percent 1-year certificates due July 31, 1959.</p> <p>Refunding announcement should assure the market that the August cash financing would be in securities with maturity of less than 1 year. Offering should be tax anticipation certificates or bills maturing in March 1959 but exact terms would depend upon amount of cash to be raised and condition of short-term market at time of offering.</p>	<p>Offered exchange for 1½-percent certificates due Aug. 1, 1959.</p> <p>Announcement made as suggested. Offered \$3,500,000,000 of 1½-percent tax anticipation certificates due Mar. 24, 1959.</p>
<p>Sept. 23.....</p>	<p>New cash of about \$3,500,000,000.</p>	<p>Offer up to \$1,000,000,000 of 3¼-percent notes due May 15, 1960; and later auction about \$2,750,000,000 of special bills due May 15, 1959.</p>	<p>Offered \$1,000,000,000 of 3¼-percent notes due Nov. 15, 1959, at par and \$2,500,000,000 special bills due May 15, 1959, at a price of 98.023 to yield 3.25 percent.</p>

Date of committee report	Financing problem	Committee recommendations	Treasury offerings
1958			
Nov. 7.....	Refunding of 3½-percent certificates due Dec. 1, 1958, and 2½ percent bonds due Dec. 15, 1958.	Offer optional exchange for certificates due in November 1959 or notes due in 4 to 5 years. Securities should be priced at rates sufficient at time of offering to avoid large attrition and with the longer issue above the shorter issue to encourage extension of debt.	Offered optional exchange into 3½ percent certificates due Nov. 15, 1959, at 99.95 percent of par or 3½ percent notes due May 15, 1961, at 99½ percent of par.
	New cash in December....	Offer \$3,000,000,000 of tax anticipation bills due June 22, 1959, on auction basis.	Offered at auction \$3,000,000,000 tax anticipation bills due June 22, 1959.
	Should part of about \$4,500,000,000 cash needed for period January to March 1959, be obtained by additional weekly bills.	Meet the problem by making offering during January-March period.	Undertook additional bill financing by introducing new cycle of both 13-week and 26-week bills.
1959			
Jan. 8.....	New cash of about \$2.25 billion.	Offer \$750 million of 4-percent bonds due Feb. 15, 1960, at price of 99 to yield 4.07 percent, and auction \$1.5 billion of tax anticipation bills due Sept. 22, 1959.	Offered \$750 million of 4-percent bonds due Feb. 15, 1960, at a price of 99 and \$2.5 billion of 3¼-percent notes due May 15, 1960, at a price of 99¼ to yield 3.45 percent.
	Preliminary recommendations on February refunding.	Under then existing conditions a 3-way optional exchange for 1-year certificates, 3-year to 5-year notes, or bonds with maturity of about 10 years.	
Jan. 29.....	Refunding of 2½-percent certificates due Feb. 14, 1959, and 1½-percent notes due Feb. 15, 1959.	Offer optional exchange for 3¼-percent certificates due Feb. 15, 1960, or 4-percent notes due Feb. 15, 1962.	Offered optional exchange for 3¼-percent certificates due Feb. 15, 1960, or 4-percent notes due Feb. 15, 1962.
Mar. 19.....	New cash of about \$4 billion.	Offer \$500 million of additional 4-percent bonds due Oct. 1, 1960, at par, \$1.5 billion 4-percent notes due May 15, 1963, at par, and approximately \$2 billion special bills due Nov. 15, 1959 at auction.	Offered \$500 million additional 4-percent bonds due Oct. 1, 1960, at par, about \$1.5 billion 4-percent notes due May 15, 1963, at par, and about \$2 billion of special bills due Jan. 15, 1960. Bill auction followed subscription closing on bonds and notes.
Apr. 19.....	Refunding of special bills and 1¼-percent certificates due May 15, 1959.	Offer holders of special bills exchange for 3½ percent tax anticipation obligations due Dec. 22, 1959, and holders of 1¼-percent certificates exchange for 3½-percent certificates due May 15, 1960, at price to yield about 4 percent.	Redeemed special bills in cash. Offered 1¼-percent certificates exchange for 4-percent certificates due May 15, 1960, at 99.95 to yield 4.05 percent.
	New cash of about \$1.5 to \$2 billion.	Auction for cash special bills due Apr. 15, 1960.	Auctioned for cash \$2 billion special bills due Apr. 15, 1960, and \$1.5 billion tax anticipation bills due Dec. 22, 1959.
June 25.....	New cash of about \$5 billion.	Auction for cash \$3 billion of tax anticipation bills due Mar. 22, 1960, and later, \$2 billion special bills due July 15, 1960.	Offered at auction \$3 billion of tax anticipation bills due Mar. 22, 1960, and \$2 billion special bills due July 15, 1960.
July 16.....	Refunding of 1½-percent certificates and 4-percent notes, due Aug. 1, 1959.	Redeem 4-percent notes in cash. Offer 1½-percent certificates optional exchange for 4½-percent issue due Aug. 1 or 15, 1960, or 4½-percent notes due May 15, 1964.	Offered notes and certificates optional exchange for 4½-percent notes due Aug. 15, 1960 or 4½-percent notes due May 15, 1964.
	New cash in August.....	Refunding announcement should state August cash financing to be limited to short-term securities maturing in less than 1 year.	(Not yet announced.)

AMERICAN BANKERS ASSOCIATION—MEMBERSHIP OF COMMITTEE ON GOVERNMENT
BORROWING, 1958-59

Robert V. Fleming (chairman)	Chairman of board, the Riggs National Bank, Washington, D.C.
Henry C. Alexander	Chairman of board, Morgan Guaranty Trust Co. of New York, New York, N.Y.
Bruce Baird	President, National Savings & Trust Co., Washington, D.C.
S. Clark Beise	President, Bank of America N.T. & S.A., San Francisco, Calif.
Kenton R. Cravens	President, Mercantile Trust Co., St. Louis, Mo.
Fred F. Florence	Chairman executive committee, Republic National Bank of Dallas, Dallas, Tex.
John M. Griffith	President, City National Bank, Taylor, Tex.
H. Frederick Hagemann, Jr.	President, Rockland-Atlas National Bank of Boston, Boston, Mass.
N. Baxter Jackson	Chairman of executive committee, Chemical Corn Exchange Bank, New York, N.Y.
David M. Kennedy	Chairman of board, Continental Illinois National Bank & Trust Co. of Chicago, Chicago, Ill.
Homer J. Livingston	President, the First National Bank of Chicago, Chicago, Ill.
John J. McCloy	Chairman of board, the Chase Manhattan Bank, New York, N.Y.
Reno Odlin	President, Puget Sound National Bank, Tacoma, Wash.
F. Raymond Peterson	Chairman of board, First National Bank of Passaic County, Paterson, N.J.
Dietrich Schmitz	Chairman of board, Washington Mutual Savings Bank, Seattle, Wash.
Earl B. Schwulst	President, the Bowery Savings Bank, New York, N.Y.
James E. Shelton	Chairman of board, Security-First National Bank of Los Angeles, Los Angeles, Calif.
Norfleet Turner	President, First National Bank of Memphis, Memphis, Tenn.
Joseph C. Welman	President, Bank of Kennett, Kennett, Mo.
A. L. M. Wiggins	Chairman of board, the Bank of Hartsville, Hartsville, S.C.
Paul I. Wren	Executive vice president, Old Colony Trust Co., 1 Federal Street, Boston, Mass.

OFFICERS AND STAFF

Lee P. Miller	President, Citizens Fidelity Bank & Trust Co., Louisville, Ky. (president of the American Bankers Association).
John W. Remington	President, Lincoln Rochester Trust Co., Rochester, N.Y. (vice president of the American Bankers Association).
Merle E. Selecman	Executive vice president, American Bankers Association, 12 East 36th Street, New York, N.Y.
Eugene C. Zorn, Jr., (secretary of the committee)	Deputy manager and director of research, American Bankers Association, 12 East 36th Street, New York, N.Y.

(The following was subsequently submitted for the record:)

CONGRESS OF THE UNITED STATES,
JOINT ECONOMIC COMMITTEE,

September 4, 1959.

Memorandum

To: Senator Paul H. Douglas, Chairman.

From: James W. Knowles, Special Economic Consultant.

Subject: Analysis of the recommendations on debt management of the Committee on Government Borrowing of the American Bankers Association to the Secretary of the Treasury.

When you inserted in the record of the committee's recent hearings exhibits setting forth the recommendations to the Secretary of the Treasury by the Committee on Government Borrowing of the American Bankers Association, together with subsequent actual Treasury offerings, you requested the staff to prepare for insertion in the record an analysis which would show the degree of agreement between the recommendation made to the Treasury and the subsequent offerings. This memorandum has been prepared for the record in accordance with your request.

In conformity with your instructions, the advice given by the American Bankers Association's Committee on Government Borrowing was compared with the subsequent offerings of the Treasury for the year 1952 and for 1953-59. Each recommendation was classified in one of four categories: (1) Advice accepted; (2) advice accepted, but with minor changes; (3) advice accepted, but with major changes; and (4) advice rejected. There is, of course, no basis in the published record for the staff to determine what the Treasury's views were on the particular offering before they met with the American Bankers Association's committee, or what offering would have been made in the absence of their advice.

Independent reviews of the record were made by different analysts and the different classifications were compared. Then a final classification was arrived at. There were only very minor differences in the results arrived at by the different analysts.

The tabulation given below shows that the Treasury rejected 19 percent of the recommendations of the American Bankers Association's committee. Its offerings were identical with, or substantially identical with, the American Bankers Association's advice in approximately three-fifths of the cases. If we include the cases where only minor changes were made in the Treasury offering from what the American Bankers Association's committee had advised, then over three-fourths of the offerings were in agreement with the advice given. Only a minor fraction of the cases represented partial acceptance of the American Bankers Association's committee's advice but with some major revision in the terms of the offering. If all cases in which the advice was accepted—whether entirely, with minor revisions, or with major revisions—are combined, then in about four-fifths of the cases the Treasury's offering was in general agreement with the advice given.

The tabulation referred to above follows:

Period	Total	Advice accepted				Advice rejected
		As given	But with minor changes	Partially but with some major changes	Total accepted	
1952:						
Number.....	19	11	1	0	12	7
Percent.....	100.0	57.9	5.3	0	63.2	36.8
1953-59:						
Number.....	84	50	17	4	71	13
Percent.....	100.0	59.5	20.2	4.8	84.5	15.5
1952-59:						
Number.....	103	61	18	4	83	20
Percent.....	100.0	59.2	17.5	3.9	80.6	19.4

Representative PATMAN. We will have our next meeting in the auditorium of the New Senate Office Building, Monday, July 27, at 10 a.m., when Mr. Martin, Chairman of the Board of Governors of the Federal Reserve System, will be our witness.

If I am not mistaken, that is in the northwest corner of the new building.

The committee stands adjourned.

(Whereupon, at 1.15 p.m., Friday, July 24, 1959, the committee adjourned, to reconvene at 10 a.m., Monday, July 27, 1959.)

EMPLOYMENT, GROWTH, AND PRICE LEVELS

MONDAY, JULY 27, 1959

CONGRESS OF THE UNITED STATES,
JOINT ECONOMIC COMMITTEE,
Washington, D.C.

The committee met at 10 a.m., pursuant to adjournment, in the auditorium, New Senate Office Building, Representative Wright Patman, vice chairman of the committee, presiding.

Present: Senators Douglas and Bush; Representatives Patman, Reuss, Coffin, Curtis, and Widnall.

Representative PATMAN. The committee will come to order. You may proceed, sir, in your own way.

But for the record, may I first say that Chairman Douglas is unable to be here this morning at the beginning of our session. He has two other committee meetings very important to him, to Chicago, and to Illinois. But he will be here as soon as possible.

STATEMENT OF WILLIAM McCHESNEY MARTIN, JR., CHAIRMAN, BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM; ACCOMPANIED BY RALPH A. YOUNG, DIRECTOR, DIVISION OF RESEARCH, FEDERAL RESERVE BOARD; WINFIELD W. RIEFLER, ASSISTANT TO THE CHAIRMAN, FEDERAL RESERVE BOARD; AND ROBERT ROOSA, VICE PRESIDENT, NEW YORK FEDERAL RESERVE BANK

Mr. MARTIN. In this opening statement, I would like to comment first on one aspect of the problem you are considering—the importance of freely competitive markets to maximum economic growth. In so doing, I do not wish to understress the importance of any other conditions necessary to healthy economic growth. Indeed, if there is one essential for sustained growth that stands out above all others, it is the maintenance of a volume of real savings and investment sufficient to support continuous renewal, adjustment, and expansion of our total capital resources. As you know, the maintenance of adequate saving and investment depends upon broadly based and justified confidence in a reasonably stable dollar.

Role of free markets: No one here would deny that free markets are essential to the vital and vigorous performance of our economy. No one would urge that we encourage monopolistic practices or administered pricing, and few would advocate Government interference with the market process as a general principle. On the contrary, nearly everyone would agree that such developments are injurious to the best use of our resources, that they distort the equitable distri-

bution of final product, and that they interfere with economic progress.

Differences of viewpoint on free markets arise only when the complexities of specific market situations make it difficult to discern whether markets are, in fact, functioning as efficiently as we might reasonably expect. Well-informed and well-intentioned observers will disagree as to whether an appropriate degree of competition exists in particular markets and, if not, as to what corrective steps, if any, it is appropriate for Government to take.

If the policies we follow in the financial field are to be fully effective in promoting growth and stability, they must be able to permeate the economy through the mechanism of efficient markets. This generalization applies to all markets, for all types of goods and services. Naturally, the Treasury and the Federal Reserve are most immediately concerned with financial markets, both because we have some direct responsibility for these markets, and because they represent the main channel through which the Government financial policies to foster growth and stability must pass.

The market for Government securities: We are especially concerned with the market for U.S. Government securities. With a Federal debt of \$285 billion, Government securities are a common and important asset in the portfolios of businesses, financial institutions, and individuals. An efficient market for Government securities is obviously needed for the functioning of our financial mechanism. We are fortunate in this country to have such a market. From the standpoint of the Federal Reserve, it is hard to conceive of the effective regulation of the reserve position of the banking system without some such facility through which to conduct open market operations of large magnitude.

The initial results of our study of this market with the Treasury are encouraging in many ways. As was pointed out in the summary of the study made available to you on Friday, huge transactions are carried out every day in an orderly fashion and at very small cost to ultimate investors. One cannot fail to be impressed by the fact that there are dealers who stand ready, at their own initiative and at their own risk, to buy or sell large blocks of securities. Frequently, single transactions run into millions of dollars. Despite the absence of any assurance that a given purchase will be followed by an offsetting sale, dealers quote bid and ask prices that typically have a spread of less than one-fourth of 1 percent on the price of long-term bonds and range down to a few one-hundredths of 1 percent on Treasury bill yields.

If you have had an opportunity to examine the preliminary study manuscripts, you are aware that they do suggest that some improvements in the Government securities market may be in order. We would hope that these improvements can be made within the framework of existing authority and through voluntary cooperation with various market participants. There is, however, a possibility that further authority might be necessary or desirable. We expect to have a clearer idea about how to accomplish desirable improvements after we have had an opportunity to consider carefully the findings of the staff study just completed last week.

There is one possible change in the organization of the Government securities market that would not, as I view it, lead to improvement.

That change would be the enforced conversion of the present over-the-counter dealer market into an organized exchange market. The reasons why this change would not be constructive or even practicable are set forth in the joint statement on the study's findings. On the other hand, any efforts on the part of existing organized exchanges to extend or strengthen the facilities now made available to buyers and sellers of Government securities should certainly be encouraged. There is no reason why better exchange facilities would not prove to be a helpful supplement to those provided by the present dealer market.

Another change affecting the Government securities market that has been suggested relates to Federal Reserve participation in it, and pertains in particular to the extension to longer term maturities of Federal Reserve open market operations. Some discussion of this suggested change is appropriate here, for it is not a matter encompassed by the Treasury-Federal Reserve study.

System operations in short-term Government securities: Since the Treasury-Federal Reserve accord in 1951, the System's day-to-day trading in Government securities has largely been in short-term issues. In 1953, after extensive reexamination of System operations in the open market, the Federal Open Market Committee formally resolved to make this a continuing practice.

I think that nearly everyone who has studied these matters would agree that the bulk of Federal Reserve operations must be conducted in short-term securities; that necessarily means largely in Treasury bills. The short-term sector of the market is where the greater part of the volume of all trading occurs. Dealer positions are characteristically and understandably concentrated in these shorter issues. Differences of view on whether System trading should extend outside the short-term area hinge upon whether or not some small part of our regular buying and selling should be done in the longer term area.

To appraise this difference in viewpoint, we need first to consider the basic economics of System open market operations. Federal Reserve operations in Government securities influence prices and yields of outstanding securities in three fundamentally different ways:

1. They change the volume of reserves otherwise available to member banks for making loans and investments or paying off debts;
2. They affect the volume of securities available for trading and investment; and
3. They influence the expectations of professional traders and investors regarding market trends.

Of these effects, the first is by far the most important. Under our fractional reserve banking system, additions to or subtractions from commercial bank reserves have a multiple expansive or contractive effect on bank lending and investing power. Other things being equal, this means that any given change in System holdings of securities will tend to be accompanied by a change in commercial bank portfolios of loans and investments several times as large. Unlike many other institutional investors, commercial banks maintain Government security portfolios with a wide maturity distribution although the largest component will be short-term securities. Hence, the major effect on market prices and interest rates will result from the actions subsequently taken by commercial banks to expand or con-

tract their asset portfolios, and the impact will be distributed throughout the market.

With regard to the effect on the availability of securities in the market, substantial System purchases or sales of short-term securities exert a minimum influence on the market supply. For example, most of the \$35 billion of bills outstanding is in the hands of potential traders. On the other hand, much the largest part of the marketable longer term issues is in the hands of permanent investors. Current trading in them is confined to a very small fraction of the outstanding volume. For this reason, the long-term area of the market shows greater temporary reaction than the short-term area to large purchase or sale orders.

Any attempt to use System operations to influence the maturity pattern of interest rates to help debt management would not, in my opinion, produce lasting benefits—I emphasize the word “lasting”—and would produce real difficulties. If an attempt were made to lower long-term interest rates by System purchases of bonds and to offset the effect on reserves by accompanying sales of short-term issues, market holdings of participants would shift by a corresponding amount from long-term securities to short ones. This process could continue until the System’s portfolio consisted largely of long-term securities. Accordingly, the System would have put itself into a frozen portfolio position.

The effect of thus endeavoring to lower long-term yields, without affecting bank reserves, would be to increase the overall liquidity of the economy. Not only would the supply of short-term issues in the market be increased, but also all Government bonds outstanding would be made more liquid because they could be more readily converted into cash. The problem of excess liquidity in the economy, already a serious one, would be intensified. The Treasury now, even with the present interest rate ceiling, would have no difficulty in reaching the same result. It has merely to issue some \$20 billion of short-term securities and use the proceeds to retire outstanding long-term debt. Fortunately, it is not contemplating any such action.

The effect of System open market operations on the expectations of market professionals can be of critical importance depending upon the market area in which the operations are conducted. In the longer term area of the market, dealers, traders, and portfolio managers are particularly sensitive to unusual changes in supply and demand. One important reason is that long-term securities are subject to wider price fluctuation relative to given changes in interest rates than are short-term issues. Therefore, trading or portfolio positions in them incur a greater price risk.

These traders and investors in long-term securities are aware that the System holds the economy’s largest single portfolio of Government securities. They also know that the System is the only investor of virtually unlimited means. Consequently, if the System regularly engaged in open market operations in longer term securities with uncertain price effects, the professionals would either withdraw from active trading or endeavor to operate on the same side of the market as they believed, rightly or wrongly, that the System was operating.

If the professionals in the market did the former, the Federal Reserve would become in fact the price and yield administrator of the long-term Government securities market. If they did the latter, the total effect might be to encourage artificially bullish or bearish expectations as to prices and yields on long-term securities. This could lead to unsustainable price and yield levels which would not reflect basic supply and demand forces. The dangerous potentialities of such a development are illustrated by the speculative building and liquidation of mid-1958, described in detail in the Treasury-Federal Reserve study.

Either of these effects would permeate, and tend to be disturbing to, the whole capital market. Accordingly, instead of working as a stabilizing force for the economy, such open market operations in long-term securities could have the opposite result. In other words, if the Federal Reserve were to intrude in the adjustment of supply and demand in order directly to influence prices and yields on long-term securities or in a way that resulted in unsustainable prices and yields, it would impair the functioning of a vitally important market process.

Some public discussion of the Federal Reserve's present practice of conducting open market operations in short-term securities implies, it seems to me, that the System has assumed an intractable and doctrinaire position on this matter. This is not a correct interpretation of what we have done. We adopted this practice after a careful study of experience and of the effects of our operations upon the market and the banking system. In this review, we were naturally mindful of the specific tasks of the System; namely, to regulate the growth of the money supply in accordance with the economy's needs and to help maintain a stable value for the dollar.

The practice or technique was adopted, not as an iron rule, but as a general procedure for the conduct of current operations. It is subject to change at any time and is formally reconsidered once each year by the Federal Open Market Committee in the light of recent experience. Exceptions can be, and have been, authorized by the Committee in situations where either Treasury financing needs, conditions in the money market, or the requirements of monetary policy call for such variations. The System, at times has been a subscriber to longer term issues in Treasury exchange offerings when appropriate, and at other times has purchased such securities in the market.

I might interject here, Mr. Patman, that the mere fact that this matter has received such discussion is well known to all the members of the Open Market Committee, and you can be sure it will be brought up by members of the Committee at each of the meetings, as a result of this. To that extent, I think this discussion is very helpful, because if we are wrong in what we are doing we certainly want to explore it and find out whether we are. But it is not an issue that is just put on the shelf and disposed of. It is not written into law.

In other words, we endeavor to apply this practice flexibly as we do all of our practices in the administration of monetary policy. As I have stated to this committee on other occasions, flexibility is an essential ingredient of our entire reserve banking operation. When reserve banking loses flexibility, it will no longer be able to do the job that is required of the central bank in the market economies of the free world.

Measurement of economic growth: Now, I think it is important that we realize the limitations as well as the usefulness of our statistical means. So, before concluding my statement, I want to mention one entirely different matter that we have been considering at the Board and that I think, has special relevance to the broad scope of this committee's interest. That is the measurement of growth. As you know, one of the most frequently used indicators of growth in the industrial sector has been the Board's index of industrial production. One of the greatest lessons we learn from the compilation of this index, which we try to do as carefully and competently as we know how, is that the mere matter of measuring growth is a very tricky thing.

As the structure of the economy keeps changing, the job of combining measures of its many parts into a single index cannot be done, despite our best efforts, without having to make major revisions every few years. We again have underway a basic revision, the final results of which will be available soon. The nub of what this revision shows is that the growth rate in the sectors covered by the Board's index has been materially greater over the past decade than has appeared from the unrevised index.

The statistical data that we have to use from month to month can only be cross-checked in a comprehensive way when we have available the results of a full census. Congress authorized the Department of Commerce to conduct one of these in 1947 and another as of 1954. The immense task of digesting and reappraising the results of these censuses, and then refitting all of the monthly data into these basic benchmarks, has now progressed far enough to indicate that the revised index, with the 1947-49 period as the starting point at 100, will show a level of around 165 at mid-1959. That is 10 points higher than the figure shown by our unrevised index for June.

Some of this difference results because we are now able to include, with appropriate proportional weight alongside other items, more of the fuel and energy production that has been going on all the time without being represented in the index. More than half of the difference, however, results from improvements in measurement of presently included industries. The monthly movements of the revised and present indexes are quite similar, so that main effect of the revision in the total is to tilt upward this measure of industrial growth over the past decade. For example, it now appears that industrial output of consumer goods on a revised basis has risen at an average annual rate of 3.8 percent as compared with 3.2 percent shown by the unrevised index for the consumer goods sector. Population growth has been at a rate of 1.7 percent per year.

Industrial production, to be sure, is only one of the ways that growth might be measured, but it is a measure in real terms and so is free of price influences. Crude measurements of growth in aggregate dollar terms can be seriously misleading, not only with respect to what the economy has done but also in marking out guidelines as to how we may reasonably expect the economy to grow in the years ahead. It is no achievement to have a rise of 10 percent in the general price level such as occurred in the months after the Korean outbreak—even though that does puff up the figures on gross national product quite handsomely. The increase of 15 percent in the current

dollar value of gross national product from 1955 to 1957 was only half of what it seemed to be, because it was inflated by a general price increase of 7 percent.

Throughout its entire history, this economy has grown by staggering magnitudes. It is because I, for one, want to do everything I can to keep it growing that I urge the maintenance of free markets and reasonably stable prices as primary objectives of public policy.

Representative PATMAN. Thank you, Mr. Martin. Will you identify the gentlemen who are accompanying you?

Mr. MARTIN. Mr. Winfield W. Riefler, on my right, is Assistant to the Chairman of the Federal Reserve Board. Mr. Robert Roosa is the vice president in charge of the division of research at the Federal Reserve Bank of New York, who has come down to help me on this. And Mr. Ralph Young is the head of our Division of Research and Statistics.

Representative PATMAN. Mr. Martin, with reference to the debacle in the Government bond market in midsummer 1958 I notice you say in your joint statement with Secretary Anderson that one of the causes of the sudden drop in bond prices was—

Expectations of tightening credit conditions, based in part on rumors of a shift in Federal Reserve policy.

Does that statement refer to the period immediately following the June 17 meeting of the Open Market Committee or the period immediately following the July 8 meeting of the Open Market Committee?

Mr. MARTIN. It might refer to either meeting, Mr. Patman, as it could have resulted from the current flow of economic information which was reflecting fairly clear improvement in business conditions.

Representative PATMAN. As I understand the report, most of the trouble was caused by the nonprofessional speculators and plungers coming into this market, mostly late in May. Is that correct?

Mr. MARTIN. Yes, late May and early June, probably.

Representative PATMAN. You would qualify it to include early June?

Mr. MARTIN. Yes, I would. Mr. Young, who has worked on the study, will be glad to speak on that.

Representative PATMAN. And a great deal of money was lost in the market. Do you know how much was lost?

Mr. MARTIN. We did not make any measurement.

Representative PATMAN. You did not make any estimate.

Does your report present any information on the profits made by either of the 17 Government securities dealers or the New York banks that financed so much of the speculative boom?

Mr. MARTIN. No, we do not have that.

Representative PATMAN. The commercial banks of the country made \$681 million in profits from speculating in securities last year, which was 10 times as much as they made in such speculations in 1957, the year before. That would indicate that the commercial banks got out of the market pretty well before the bubble burst, would it not, Mr. Martin?

Mr. MARTIN. The fact that they made these profits?

Representative PATMAN. The fact that they made such enormous profits would indicate that they must have gotten out before the

bubble burst; are bound to have done so, because they would not have made such profits.

And remember that these profits were made not by the 13,000 commercial banks so much as by 2 percent of the commercial banks, that made over 66 $\frac{2}{3}$ percent of the \$681 million profits. The very fact that these few banks were able to make such an enormous amount indicates clearly, does it not, that they must have gotten out before the bubble burst?

Mr. MARTIN. The decline in interest rates was a major factor in making their portfolios attractive and profitable.

We have a table, Mr. Patman, that shows that over the period from 1951 to date, taking these profits and offsetting them against losses, there was a net loss to the banks of \$87 million. I believe that is correct.

Representative PATMAN. I am not talking about that. That is something else. I am talking about profits on Government securities last year, 1958—

Mr. MARTIN. That is what I am talking about.

Representative PATMAN. That the banks made in trading or speculating, whichever you want to call it, on Government securities.

Mr. MARTIN. This table, which we will put in the record, refers to Government securities.

Representative PATMAN. That is right. \$681 million for all banks; \$612 million for member banks.

(The table referred to follows:)

JULY 27, 1959.

Profits, recoveries, and losses on securities, member banks, 1951-58

[In millions of dollars]

	Profits	Recoveries	Losses and chargeoffs	Net (other than transfers to or from reserves)
1951.....	52	16	88	-20
1952.....	29	14	108	-65
1953.....	35	11	174	-128
1954.....	375	15	74	+316
1955.....	51	21	261	-189
1956.....	28	16	369	-325
1957.....	57	10	278	-211
1958.....	612	17	94	+535
Total.....	1,239	120	1,446	-87

Source: Federal Reserve Bulletin (p. 650, June 1959; p. 564, May 1955).

Mr. MARTIN. At this particular time those are nonrecurring profits, and when you have a market that turns over in a year \$200 billion worth of securities, there does not seem to be anything particularly startling.

Representative PATMAN. It does not disturb you at all? It does not excite your curiosity?

Mr. MARTIN. No.

Representative PATMAN. Does it excite your curiosity when it looks like it is following a pattern, Mr. Martin? In 1953 Government bonds were forced down in price, and the banks bought them up. Then in 1954, when they were forced up again or went up again in

price, the banks unloaded and they made over \$400 million profit that time, 2 percent of the banks making two-thirds of it. Then in 1957 they go way down again and the banks buy them again. In 1958, in the early part, they go up again and the banks sell and make \$681 million. It looks now as if they are making that cycle 2 years instead of 4, by running them down in 1959, probably with the expectation of running them up in 1960 and duplicating that enormous profit.

Mr. MARTIN. We do not know what the book losses of these securities are at the end of each year. From the complaints that I get from bankers, they are pretty worried from time to time about their portfolio losses.

Representative PATMAN. Worried about them? They get 100 percent deduction for losses on them, do they not, whether it is 2 days, 2 weeks, or 6 months? That is correct, is it not?

Mr. MARTIN. Deduction from what?

Representative PATMAN. That is, taxwise, for tax losses.

Mr. MARTIN. Well, they offset them as anyone else does.

Representative PATMAN. No; the banks have a special law taxwise for themselves.

Mr. MARTIN. Oh, yes; that is right.

Representative PATMAN. They have a privilege that no other individual or corporation has; that is correct, is it not?

Mr. MARTIN. Yes; that is right.

Representative PATMAN. The profits of most of the dealers I find are not publicly reported, but in trying to look them up I find that one of them, probably the biggest one, is a corporation and reported its profits to Standard & Poor's. According to Standard & Poor's, the Discount Corp. made a net profit of \$1,803,585 in 1958. That was 55 percent more than they made in the previous year. So would it be safe to assume that The Discount Corp. had unloaded its holding before the big price break?

Mr. MARTIN. You could not tell from that alone, but unquestionably they profited during that period, Mr. Patman. They were in business for profit, and they can be expected to take advantage of every situation they can.

Representative PATMAN. Do you think, Mr. Martin, that there was any evidence of leaks disclosed in your investigation?

Mr. MARTIN. We have done our level best to find any evidence of that, but we found no indication of them.

Representative PATMAN. You found no indication of leaks?

Mr. MARTIN. None whatsoever.

Representative PATMAN. This \$681 million in profits realized by the commercial banks 2 percent of the banks realizing two-thirds of the profits, necessarily does not include all the people that have the benefit of any information that these banks have or had and enabled them to make such huge profits.

The \$681 million would be profits of the banks, but, of course, corporations and individuals entered into that. So the question of leaks I think would be a very important one.

How do you explain the fact that there are no leaks and no inside information, when the whole account of the Federal Reserve System, the open market account, is conducted there in New York under the auspices, the direction, and the administration and by an official

selected by the Federal Reserve Bank of New York, when that bank is operated by nine directors, six of whom are selected by the private banks? Naturally, they would have access to these officials whom they have selected to carry out the duties of the banks, they would have some contacts with them, and certain information necessarily they would get.

I would just like you to explain how it is possible to keep down leaks and inside information under those facts, Mr. Martin, and particularly in view of the fact that you do not even have a rule or law against people who are making these policies from investing in, or speculating in the Government bond market themselves.

Mr. MARTIN. Mr. Patman, you will recall that we have been over this with you in public hearings before. We have found from a good deal of study of this problem that we do not know any way you can positively legislate honesty.

In the administration of this account, this manager that you are talking about is approved by the Federal Open Market Committee.

Representative PATMAN. Of course, I know you say that, but is that very important?

Mr. MARTIN. Yes.

Representative PATMAN. As to the fact that he is a good man, and he is, of course, you would accept him, and if you did not accept him for any personal or other reason, they would have another man just as good. So you have a veto power, but that does not give you much power over the man, Mr. Martin.

Mr. MARTIN. We always have the power of removal in the final analysis if we wish to exercise it. I grant you this is a difficult road to take.

Representative PATMAN. On that part I do not exactly see eye to eye with you. How would you remove him?

Mr. MARTIN. We could deny salary, for one thing. I do not think he would stay very long if he did not get paid.

Representative PATMAN. I have not heard of your doing that in any case.

Mr. MARTIN. We have not had any reason for doing it.

Representative PATMAN. That is pretty remote, is it not?

Mr. MARTIN. We do have the power, however.

This matter of the possibility of leaks and the composition of the Federal Reserve System as provided by statute is a difficult one. They have had that problem in England. You have been over there and visited with them and know that they had a tribunal that worked on it; also, they have had the Radcliffe Committee which will have a commission report before too long. I do not know what their hearings will reveal. There are advantages and disadvantages in all of these setups.

We try to bring to bear the best minds and the best judgment that we can get on these problems. I confess to you, as I have in some of our exchanges before, that there are some things that I have worried about in the System with respect to the possibility of leaks. We are doing everything in our power to correct any problems in this area.

Of our nine directors, three are appointed by the Board and six of them are elected through this process of proportional interest in the System through the subscriptions to capital of the Reserve banks.

That was the device worked out by Congress years ago. It is true that three of those are bankers—one represents a large bank, one a medium-sized bank, and one a small bank—and three of them are industrialists.

Representative PATMAN. And they may be bankers, too.

Mr. MARTIN. No; I do not believe so.

Representative PATMAN. May I remind you, Mr. Martin, that we had an exchange about that one time; I asked you to get a statement from each one of these class B directors, and over half of them had bank stock at that time.

Mr. MARTIN. Yes, but they were not bankers, Mr. Patman.

Representative PATMAN. I know, but they owned bank stock.

Mr. MARTIN. Some of them owned bank stock; not many, but a few did.

Representative PATMAN. I will agree with you that to that extent only are they bankers.

Mr. MARTIN. Yes, only through the ownership of stock.

That has been our device for bringing this to bear.

Now, there have been questions raised from time to time, particularly in the New York Reserve bank, because of its proximity to the open market, and because of the fact that it is close to the major money market, that has placed a particular responsibility on those directors not to use any information that they may receive at the bank.

It has been my judgment that those directors have leaned over backwards to avoid it. Nevertheless, I confess to you that it has concerned me some, and I think that is something we ought always to continue to study very carefully, and maybe Congress will want to change it someday.

Representative PATMAN. Thank you, sir. My time has expired, but I just want to ask you one more question.

In sending out your questionnaire to the 17 dealers, did you collect any information on their profits at all?

Mr. MARTIN. We did not.

Representative PATMAN. Mr. Reuss.

Representative REUSS. Governor Martin, 2 or 3 weeks ago the House Ways and Means Committee tentatively approved a piece of legislation lifting the 4¼ percent ceiling for 2 years on Treasury bonds and containing the so-called sense-of-Congress resolution or amendment. I am sure you are familiar with it, but it is so short that I will restate it:

It is the sense of Congress that the Federal Reserve System, while pursuing its primary mission of administering a sound monetary policy, should to the maximum extent consistent therewith utilize such methods as will assist in the economical and efficient management of the public debt, and that the System where feasible should bring about future needed monetary expansion by purchasing United States securities, of varying maturities.

Naturally I was very interested in the reaction of the Federal Reserve System to that. I read some stories in the newspapers about what it might be, but nothing official until in Friday's newspaper there was reported that the System over your signature had stated its position on that in a letter sent to the Republican members of the House Committee on Ways and Means.

I think we Democrats would like to know it, too. Would you, therefore, produce a copy of that letter?

Mr. MARTIN. I would. As the letter states, I gave a copy of it to Chairman Mills of the House Ways and Means Committee simultaneously with giving it to Mr. Simpson, who asked for a letter. I do not know that I brought a copy with me.

Representative REUSS. Would you have one of your associates get a copy?

Mr. MARTIN. I will do that, and have copies distributed. I shall be glad to.

Representative REUSS. Can we do something about getting a copy of that right now so that we can discuss it?

Mr. MARTIN. Yes. (See p. 1287.)

Representative REUSS. That is a letter sent to the Republican members of the House Committee on Ways and Means, according to the press.

Until we get them, Mr. Chairman, let me ask you some general questions about that sense-of-Congress resolution.

Where the Federal Reserve System determines that the money supply, for good and sufficient reasons, should be expanded, the same monetary effect is obtained, is it not, whether the expansion occurs by lowering bank reserve requirements or by purchases of U.S. securities?

Mr. MARTIN. Ultimately, but not necessarily during the flow of the money stream, because it varies at different times.

Let me put it this way: We have used a reduction in reserve requirements on occasion to actually help the Treasury, because we knew they were coming to the market at a particular time.

Representative REUSS. I understand this. Reduced reserve requirements give banks more credit-creating capacity, not only to make loans but to make investments, and included in investments are U.S. securities.

But let us just take a situation where, for good and sufficient reasons, the Federal Reserve determines that it wants to increase bank reserves by \$1 billion, picking that figure out of the air. Whether it does that by reducing bank reserve requirements in an amount equal to \$1 billion of new reserves or whether it does it by purchasing \$1 billion worth of U.S. securities is equal, from the standpoint of monetary policy; is it not?

Mr. MARTIN. Mathematically the same, but as it permeates through the System, not the same, because one of the reasons for using reserve requirements is to give all the banks in the country a little bit of reserve at a given time.

Ultimately the reserves will get distributed broadly among the banks when we purchase securities, but they do not permeate directly or as rapidly to the banking system as a whole as when we reduce reserve requirements.

Representative REUSS. But from the standpoint of the economy as a whole it is precisely identical; is it not?

Mr. MARTIN. In the ultimate effect on the reserves; yes.

Representative REUSS. And, therefore, from the standpoint of the monetary policy; that is, fighting inflation or producing an expansion of the money supply, as the case may be—the two actions are substantially equivalent; are they not?

Mr. MARTIN. Ultimately, they will have the same result.

Representative REUSS. You would not call a fellow an engineer of inflation or a funny-money fellow or a printing-press money man if, where you were prepared to increase the total money supply \$1 billion by the lowering of bank reserve requirements, he, while agreeing that the total money supply ought to be increased to the very nickel, as you suggested, and not one nickel more, nevertheless suggested doing it by purchase of U.S. securities? There is no printing press involved there; is there?

Mr. MARTIN. No; no printing press except in the atmosphere in which you are operating, and assuming what your policy is, Mr. Reuss. You see, that is where a little difficulty exists on this.

I have followed your letters and tried to answer them as cooperatively as I can, because I am sure you are sincere in this and are trying to be helpful. But what we are dealing with at the moment is an atmosphere, a very serious inflation atmosphere, one which I think is extremely serious for the country. A great many people are getting the idea that they ought not to invest in fixed securities at all; that they ought to just buy common stocks and get rich.

Representative REUSS. I know all that, and I do not yield to you, Mr. Chairman, in my detestation of inflation.

Mr. MARTIN. I know you do not.

Representative REUSS. What we are concerned with here is a common, sensible analysis of just what this act of the Ways and Means Committee says, so that, step 1, I take it that you and I are agreed that a billion dollars is a billion dollars, and that one method of adding it to the money supply is no more inflationary and no less inflationary than adding to it by another method. Is that correct?

Mr. MARTIN. I think in mathematical terms, yes, but I want to reemphasize that the flexibility of monetary policy revolves around how it is interpreted as well as what actually is achieved by it.

We have to mop up and take out constantly, and I think the real heart of your amendment is—I think we can correctly call it your amendment—you do not think that your method is inflationary; and I think that under present conditions it would be.

Representative REUSS. That is right; and all I ask is that you give me some reasons. Let us start right in on that.

Why, though it is mathematically equal, is a determination by the Federal Reserve to do what it can, consistent with sound monetary policy; to help the Treasury and the taxpayer, inflationary?

Mr. MARTIN. Let me try to put it in the proper setting.

The economical and efficient management of the Treasury debt is one of the primary concerns of the Federal Reserve, and has been at all times since I have been there.

Representative REUSS. Then you do not object to Congress telling you what you say you have been doing all the time.

Mr. MARTIN. The question is, if there is an inference that we have not been doing it, which I think there is in this amendment, I think it is unfortunate.

Representative REUSS. There is such an inference, and I want as one of the authors, to indicate a participation in it.

Mr. MARTIN. These were executive sessions of the Ways and Means Committee, and I am trying to be careful not to just spread out what was developed in that Ways and Means Committee meeting. Per-

haps it is all right now, since more of it has already come out, but I found quite definitely that there was this criticism and that there was some feeling that we had produced the situation in which the Treasury presently felt it was.

I do not think so. I think we have been conducting our affairs where, if there is a reasonable doubt of how successful we have been—and no one was talking along these lines—perhaps we should have had tighter money instead of easier money. That is the framework in which we are presently working.

Representative REUSS. Your remarks, Mr. Chairman, show that you are introducing entirely extraneous matter into this resolution. I, as its author, have explained many times, it has nothing to do with another controversy; namely, have you been increasing money supply fast enough? There are those who think you have not; there are those who think you have been increasing it too fast, although they are not many. That has nothing to do with this amendment. This amendment simply says to the extent that you decide to increase it at all, do it in a way differently, for the next 2 years, from the way you have been doing it, and from the way the Federal Reserve has testified it wants to continue to do it; i.e., the Federal Reserve in the last 5 or 6 years has increased the money supply, when it has, by the device of lowering bank reserve requirements.

The suggestion of the sense-of-Congress-amendment is that for the period of the 2 years, the Fed effect such increases as it believes should be made by the device of purchasing U.S. securities.

Let me go on with that and ask you whether, if the Federal Reserve purchased a billion dollars worth of securities, thus adding to the money supply by the amount that it wants to add, is not that a benefit to the taxpayers over the Federal Reserve's not purchasing that particular billion dollars worth of securities, deriving from the fact that the Federal Reserve's profits go back into the Treasury?

Mr. MARTIN. Mr. Reuss, we do not ever operate the System account, and never should in my judgment, to make money for the Treasury Department or the Federal Reserve.

Representative REUSS. I know that. That is precisely my objection.

Mr. MARTIN. We are trying to exercise our influence in the money stream in terms of the public welfare of the country.

Representative REUSS. Then your answer, Mr. Martin, on this point, is yes, it does make money for the taxpayers and for the Treasury if the Federal Reserve owns a particular billion dollars worth of securities, over its not owning that billion dollars worth of securities, but helping the taxpayers and the Treasury is not one of your reasons for existence?

Mr. MARTIN. It is not one of our reasons for existence. What we are trying to do is to use the money supply for the benefit of everyone.

We could make money for the Treasury—the bills are higher than the long-term securities at the present time—by just acquiring bills, and in that case we would be acquiring more earnings for the Treasury ultimately. What we are trying to do is to have a money stream that is as effective as we can have it in terms of end cost.

Let me pursue this, because I think you and I have a honest difference of opinion here that is important, and it is not a question of arrogance or intellectual defiance of the Congress. I have never been

defiant or arrogant with respect to the Congress. It is a question, though, of principle with respect to discretion in the management of the money supply.

Representative REUSS. Mr. Chairman, I agree with both your characterization of your demeanor, which I have never found arrogant, and your statement of general principles here. But I want to get an answer to my specific question, which is a simple one, and it is going to be followed by others, and it is this:

Would it not save money for the Treasury and for the taxpayers if, in a given case, the Federal Reserve purchased a billion dollars worth of U.S. securities rather than letting somebody else purchase them?

Mr. MARTIN. Let me answer you this way. Mathematically, at that particular point, yes. But if inflation is produced in that way, any saving would be microscopic. That is really the heart of what we are dealing with.

Representative REUSS. I am told my time is up, Mr. Chairman. I will return later.

Representative PATMAN. Mr. Curtis.

Representative CURTIS. Mr. Chairman, thank you.

First, Mr. Martin, our staff prepared for us what I thought was an excellent statement of some of the problems involved in this presentation, evaluating argument pro and con. I do not believe you have had the advantage of seeing that analysis. It raises five particular points: (1) The Federal Reserve "bills-only policy," which your paper today comments on to some degree; (2) the Federal Reserve "swapping operations;" (3) providing for long-run growth of the money supply and the reasons behind that, and whether or not the Federal Reserve can or should contribute to that; (4) the problem of the interest rate ceiling; and (5) the auction technique for marketing Treasury securities.

I have checked with the staff to be sure that this is in proper form. I might request the committee to turn it over to you for your comments on the pros and cons of it and to supply that commentary for the record.

Mr. Chairman, I would like to make the request that the staff do a little editing on this, which I understand they can do, there is not much that needs to be done, and that it be sent to Mr. Martin for his comments for the record.

Representative PATMAN. Without objection, it is so ordered.

Mr. MARTIN. I shall be very glad to do so.

(The material referred to is as follows:)

To: Members of the Joint Economic Committee.

From: Otto Eckstein and John Kareken.

Subject: Joint Economic Committee Hearings on the Government's Management of Its Monetary, Fiscal, and Debt Operations.

Attached are some materials which have been prepared as background information for the hearings. First, there is a memo which outlines briefly some of the topics which can fruitfully be developed in these hearings. Then there are several memos which develop briefly several topics of current interest:

1. The Federal Reserve's "bills only" policy.
2. Federal Reserve "swapping" operations.
3. Providing for long-run growth of the money supply.
4. The interest rate ceiling.
5. The auction technique for marketing Treasury securities.

Finally, there are also attached indexed sets of charts, taken from the Federal Reserve chart books, which are intended to supply the basic data pertaining to the issues which are likely to be developed in the hearings. The first

set of charts covers the period 1952 to the present, and includes information on commercial banks, interest rates, financial institutions, the public debt, and private debt. The second set of charts covers a longer period, in some cases from 1900 to the present, and includes information on Federal Reserve credit and the money supply, commercial banks, interest rates, financial institutions, the public debt, and private debt.

JULY 13, 1959.

To: Members of the Joint Economic Committee.

From: Otto Eckstein and John Kareken.

Subject: A background memo on the Joint Economic Committee Hearings on the Government's Management of Its Monetary, Fiscal, and Debt Operations.

INTRODUCTION

Events of the past 2 years—for example, the behavior of the Treasury bond market in 1957–58 and the recent Treasury request for removal of the statutory interest rate ceiling—indicate the desirability of developing in the coming hearings testimony covering the following topics:

1. The proper degree of monetary restraint.
2. The appropriate criterion (or criteria) for managing the public debt.
3. The technical problem of marketing the public debt.
4. The place of Treasury securities in the portfolios of private lenders.
5. The performance of the market for Treasury securities, with special reference to the behavior of dealers in Treasury securities and of the Federal Reserve.

1. The proper degree of monetary restraint

The money markets have, so to speak, forced the Treasury's hand. With market conditions what they are and with the existing statutory interest rate ceiling, it is unlikely that the Treasury will be able to borrow significant amounts in the intermediate and long-term markets. That interest rates are so high relatively is a serious matter, and the occasion of the Treasury's request for the removal of the statutory ceiling can be used to raise the question of whether or not we are relying too much on monetary policy to achieve economic (cyclical) stability.

Higher interest rates suggest an income redistribution, both as between creditors and debtors generally, and as between taxpayers and holders of Treasury securities. Within a rigid balance budget framework, they also suggest that other governmental programs may suffer. Greater use of fiscal policy, on the other hand, could avoid these and other consequences of high interest rates, for with greater fiscal restraint, lower interest rates would not mean inflation.

The fundamental question, therefore, is whether or not it would be better, even though it might appear to "hurt" more, to make greater use of countercyclical fiscal policy so that monetary policy need not be carried to an extreme?

2. The appropriate criterion (or criteria) for managing the public debt

For some time now the Treasury has insisted that the issuance of long-term debt is essential to any anti-inflation program. The Treasury has largely failed in its attempt to lengthen the debt maturity, and yet it is this attempt as much as anything else which accounts for the difficulties it has had in managing its refunding and new money issues.

It would be well, therefore, to know the official rationale for this policy. Is it the ordinary rationale of countercyclical debt management policy, or something else?

In a word, what is it that is expected of this attempt to lengthen the maturity of the debt, even in boom times? And is it likely that the expected benefits do in fact outweigh the costs involved? Might it not be better for the Treasury to follow a narrower policy of simply minimizing the cost (operating cost as well as interest cost) of its debt operations, and leave to the Federal Reserve the task of keeping the right maturity mix in the market?

3. The technical problem of marketing the public debt

Whatever the general level of interest rates happens to be, and whatever the criterion used in managing the debt, there is still the problem of marketing the debt in the most efficient way. Present marketing arrangements date from a long time ago, and are patterned after private underwriting techniques, except

in the very important respect that private underwriters engage in temporary support operations, whereas the Treasury has no such help. The question naturally arises, then, of whether or not the present arrangements are the best arrangements.

Might it not be better, for example, for the Treasury to rely more on the auction technique in marketing intermediate and longer term issues? (Would this switch of techniques have the effect of making the Federal Reserve less conscious of its own contribution to the Treasury's debt management problem?)

And might it not be better, insofar as it is possible, for the Treasury to plan financings further into the future, thus making it possible to float smaller issues more regularly? This may require the Treasury to carry a larger cash balance at some times, but this could be less costly than having to go to the market at an inopportune moment. Or it may require temporary use of the line-of-credit which by law the Federal Reserve extends to the Treasury; again, the gain may offset whatever disadvantages there are connected with the use of this option.

Finally, and most importantly, might it not be better if the Federal Reserve took on once again the task of offering temporary underwriting support for Treasury operations? Of course, this would require that the Federal Reserve abandon its "bills only" policy, but it would not require a return to a regime of pegged interest rates, for by its very nature underwriting support is temporary and not rigid.

4. The place of Treasury securities in the portfolios of private lenders

Some economists and market professionals feel that there has been a progressive "deterioration" in the competitive position of Treasury securities. These people suggest that it is this factor which accounts for the Treasury's difficulties associated with its attempt to market long-term bonds, and which can account for an ever-narrowing gap between interest rates paid on Treasury securities and on other types of assets in which private lenders, institutions, and individuals can invest.

It is essential, first, to determine the actual extent of this apparent deterioration of the competitive position of Treasury securities (particularly long term). There is then, assuming this deterioration to be a fact, the task of accounting for it; that is, why if at all, have private lenders changed their minds about the advantages of Treasury intermediate and longer term securities? Is it simply that there are outstanding too many Treasury securities relative to the needs of private lenders? Or, as is more likely, have Government guarantee programs, which insure not only certain kinds of mortgages against default but also certain kinds of assets (for example, savings and loan shares) which households can choose in place of savings bonds, made Treasury securities less distinctive from the risk viewpoint.

Or is it, as is often alleged, that Treasury securities are simply suffering the fate of all fixed-income obligations in times of rising prices? If so, then any increased freedom for institutional investors to hold equities can be expected to worsen the Treasury's problem.

Or, finally, is it that investors are becoming more and more aware of the risk of capital loss which has attached to Treasury securities increasingly since the time of the Treasury-Federal Reserve accord?

5. The performance of the market for Treasury securities

The movement of Treasury securities prices during 1957-58 demonstrated that this market for Treasury obligations is capable of great instability. It remains to be determined, however, precisely what factor or factors caused the sharp increase in prices and the subsequent even sharper decrease. For if price fluctuations such as these are likely to occur again, then the question is immediately posed as to whether or not they should as a matter of public policy be tolerated.

Many, many subsidiary lines of inquiry, too numerous to be mentioned here, are opened up by the two basic questions given above. In large part, this is because we know so little about the actual functioning of the market for Treasury securities; hence, almost any question is appropriate. Of prime importance, however, is the matter of the contribution of dealers' activities to the recent "speculative excesses." This is a specific aspect of a general problem: Whether in general dealers' activities are stabilizing or destabilizing.

It would also be of considerable interest to investigate whether or not any other institutional investors played a major role in the market developments of 1957-58 (for example, commercial banks). And, finally, there is the question

of current market practices—such things as the margining of securities positions, and the use of repurchase agreements to finance holdings of securities—and their contribution to market stability and instability.

Coming then to the matter of public policy with respect to market behavior, we run again into the Federal Reserve's "bills only" policy. But before considering this policy in relation to last year's market developments, one other question must be mentioned: Namely, whether or not the Federal Reserve should try to encourage dealers in Treasury securities, by whatever means are necessary, to take some responsibility for stabilizing the market in which they operate?

The fact remains, however, that the Federal Reserve has within its own power the ability to minimize price movements in the market for Treasury issues. The important questions thus relate to the Federal Reserve's exercise of this ability. For example, what criteria does it use to determine whether or not the market is "disorderly"? What criteria did it use in 1958, when it temporarily relaxed its preference for trading only in Treasury bills? What did it expect to accomplish by this relaxation? And what did it accomplish?

These questions pertain to our most recent experience, but the "bills only" policy is of more general significance, and hence raises more general issues. There is, for example, the question of just what Federal Reserve officials think of as a "good" market, and what adequate market performance is. And last, but not least, there is the matter of experience over the whole history of this policy (that is, since mid-1953): Of whether or not this policy has accomplished what was claimed for it; namely, result in a stronger market for Treasury securities.

JULY 17, 1959.

To: Members of the Joint Economic Committee.

From: Otto Eckstein and John Kareken.

Subject: A background memo on the Federal Reserve's "bills only" policy.

A. THE PREACCORD SITUATION

In order to finance World War II efficiently, the Treasury and the Federal Reserve agreed early in 1942 that the latter would hold all interest rates on Treasury securities at fixed levels; in other words, the System took on the job of "pegging" the market for Treasury securities. Of course, it was recognized at that time that this pegging operation would tie the System's hands, but this consideration was subordinated to the needs of wartime finance.

B. THE ACCORD

The pegged markets were continued far into the postwar period. But whereas this arrangement made considerable sense during the war and the reconversion period, it made much less sense after 1947; as the years went by, the Federal Reserve's power was continuously curbed even though the forces of economic expansion were gathering strength. Thus, in March 1951, the Treasury and the Federal Reserve reached their famous "accord," which returned to the System the power to regulate the money supply.

C. BEYOND THE ACCORD: THE POLICY OF MINIMUM INTERVENTION

Having the freedom granted it by the accord, the Federal Reserve continued after mid-1951 to move its policy in the direction of less and less direct intervention in the market. In late 1952 and early 1953 it put into effect the so-called policy of minimum intervention, which included the much-discussed "bills only" policy. The policy of minimum intervention is made up of the following principles:

1. The System should buy or sell Treasury securities only to influence bank reserves in accordance with general policy, and not to influence the interest rate on a particular type of security, except when the market becomes "disorderly";
2. System open-market operations should be conducted entirely in short-term securities, preferably bills, and the open-market account should not engage in "swapping" operations (for example, trading a block of bonds for an equal volume of bills);
3. No direct support should be given Treasury financing operations.

D. ACTIONS TAKEN COUNTER TO THE DOCTRINE

The policy of minimum intervention has not been always adhered to, but there have been only three occasions when the System has violated the above principles. In December 1955 the System bought certificates as well as bills in support of a Treasury financing. In the first part of 1957, the Federal Reserve sold certificates, presumably because it was almost out of bills. In July 1958, a relatively large volume of Treasury securities of different maturities was purchased in support of securities prices.

E. THE ARGUMENTS IN DEFENSE OF BILLS ONLY

Those arguments which have been set down on paper, and may therefore be taken as official, are:

1. That private decisions about investment and spending should be made on the basis of a structure of interest rates which are determined, not by the System, but by the free market.

2. That the private market for Treasury securities can only be made strong enough to support necessary System open-market operations if dealers are guaranteed against arbitrary official actions. This guarantee is given by "bills only."

3. That sales or purchases of long-term securities give rise to pronounced expectations about future interest rates, and are therefore more likely to obscure the "true" supply-demand relationship and so mislead the System into an incorrect policy.

An unofficial, but nonetheless oft-heard argument is that if the System deals in securities other than bills—

(a) It is much easier, as a matter of politics, to return again to a world of pegged interest rates; and

(b) Policy may really be made in New York, at the open-market trading desk, for policy directives from the Federal Open Market Committee can never be sufficiently detailed to guide fully actual open-market purchases and sales.

F. THE ARGUMENTS AGAINST "BILLS ONLY"

1. Leaving the determination of interest rates entirely to the free market sometimes means speculative excesses, which is why official intervention is occasionally required, even in the long-term securities markets. (See point D. above.)

2. Because the flow of funds between the long- and short-term markets is anything but free and easy, operations in bills produce gluts and stringencies in the short-term market but have only a delayed influence on long-term interest rates; moreover, the response of long-term interest rates to open-market operations in bills is extremely difficult to predict, except when bill operations are very large and hence dangerous for other reasons.

3. A strong market for Treasury securities can be best achieved by a policy which maintains relatively stable securities prices and thus encourages investment by all types of private lenders, not merely dealers in Treasury securities.

4. The "bills only" policy denies the Treasury the type of underwriting support which is employed in private financing operations.

JULY 18, 1959.

To: Members of the Joint Economic Committee.

From: Otto Eckstein and John Kareken.

Subject: A background memo on Federal Reserve swapping operations.

A. THE SIGNIFICANCE OF THE SWAPPING OPERATION

A "swapping" operation is, by definition, simply a trade of Treasury securities of different maturities by the Federal Reserve which leaves its total holdings of such securities unaffected. For example, the System Open Market Account might buy X billion dollars worth of Treasury bonds and simultaneously sell X billion dollars worth of Treasury bills. Under reasonable assumptions, therefore, the impact of this sort of swapping operation on bank reserves is zero. But the impact on relative interest rates (that is, the difference between the rates on bills and bonds) is not zero; a simultaneous sale of bills and purchase of bonds will increase the bill rate and decrease the going interest rate on bonds.

It is this combination of properties—neutrality with respect to bank reserves, but not with respect to relative interest rates—which makes the swapping operation of such potential usefulness as a tool of monetary control even during periods of inflationary pressures. Specifically, it can be used to support a particular sector of the market for Treasury securities when the economy is expanding because the support will not produce more bank reserves.

B. SOME EXAMPLES

Our own postwar history demonstrates how the swapping operation works out in practice. For example, in the latter part of 1947 Treasury bond prices began to fall, partly as a response to previous speculative activity; in December 1947 and thereafter downward pressure was even greater, for the Federal Reserve lowered its bond support price. To prevent bond prices from falling very considerably the System had to buy large quantities of bonds. But because it was able to sell large amounts of bills at the same time, total System holdings of Treasury securities rose by much less than otherwise would have been the case.

Nor is this the only example of swapping operations. We have another, though opposite, instance in the 1948-49 recession when the System sold bonds to offset bill purchases—just as it did in a limited way in the early postwar period. Indeed, bank reserves were expanded so little in the period before the Treasury-Federal Reserve accord in large part because the System made so much use of swapping operations.¹

C. SWAPPING OPERATIONS AND "BILLS ONLY"

It must be emphasized that the possibility of making greater use of swapping operations currently—for example, to ease the downward pressure on Treasury bond prices which exists today—cannot be separated from the question of whether or not "bills only" is a wise policy. Limiting open-market operations to short-term securities, preferably bills, obviously precludes the kind of swapping operations used in the past. Moreover, the broad Federal Reserve philosophy of minimum intervention includes as one of its principles an explicit prohibition against swaps. And the reason given for this prohibition is essentially that given for the entire doctrine of minimum intervention; when it adopted this prohibition (December 1953) the Federal Open Market Committee argued:

"* * * if the System open market account were to engage in purchases and sales in the open market without altering total holdings of securities in the portfolio, the objective of such transactions would not be clearly discernible to the market and thus might cause confusion and uncertainty as to credit and, in so doing, militate against the depth, breadth and resiliency sought in the Government securities market" (40th Annual Report of the Board of Governors of the Federal Reserve System, p. 104).

Again, then, swapping operations cannot be undertaken so long as bills only is in force. Or put another way, if swapping operations are desirable, then bills only cannot be a wise policy.

D. THE CURRENT APPLICABILITY OF SWAPPING OPERATIONS

Today, of course, the natural question is whether or not this type of open-market operation by the Federal Reserve represents an alternative to raising the ceiling on Treasury bonds. What this would mean presumably is that instead of having Congress remove the interest ceiling, the system would buy long-term Treasury securities in the open market and simultaneously sell short-term obligations, thus lowering long-term rates relative to short-term rates and easing the way for long-term Treasury financing. Equivalently, the system could purchase Treasury bonds directly on issue. Either procedure has the same effect, however, as short-term Treasury financing. Therefore, no answer can be given to the question of using swapping operations before it is decided whether countercyclical debt management is wise or foolish—that is, whether issuing long-term securities during periods of economic expansion is wise or foolish.

¹ It must be remembered, however, that during much of the preaccord period, particularly in the early postwar years, debt retirement went on at a goodly pace; this helped make it possible for the System to support a segment of the Treasury market without creating unwanted bank reserves.

But this is not all there is to this matter. Some economists doubt that the problem of the interest rate ceiling would have arisen at all if in 1958, when Treasury bond prices started to fall, the Federal Reserve had quickly given some temporary support to this sector of the market by means of a swapping operation. These economists argue that even small purchases of bonds (fully offset, say, by sales of bills) would have broken the force of what was essentially a speculative movement. They argue further that such action would have in no way involved a return to pegged markets, and that long-term interest rates would be lower today if appropriate action had been taken in 1958. Whether or not this argument is true is a difficult matter to decide, but it is a widely held point of view.

JULY 20, 1959.

To: Members of the Joint Economic Committee.

From: Otto Eckstein and John Kareken.

Subject: A background memo on alternative ways of expanding the money supply to accompany the growth of real output.

A. INTRODUCTION

There may be no rigid relationship between real output, the price level and the money supply, but it is nevertheless true that as the production of goods and services increases so must the money supply. Nor is such a growth in bank deposits inflationary. Quite the opposite, it is intended as a means of avoiding deflation and the interruption of economic growth.

The question therefore is how best to provide for this long-run increase in the money supply. Two possibilities should be considered: (1) a gradual reduction in reserve requirements, and (2) a gradual expansion of the Federal Reserve's holdings of Treasury securities. Both methods can be used to produce just the desired potential expansion, so the decision as to which to use must be decided on other grounds.

B. THE ISSUES

In one sense, the problem of which method to use is very topical. Some of the issues on which the choice turns have been the subject of debate both in the recent hearings of the House of Representatives Committee on Ways and Means on the interest rate ceiling and in the consideration of the bill (S. 1120) to amend the National Bank and Federal Reserve Acts with respect to required reserves. Here, however, the choice problem is considered only in the context of long-run changes in the money supply, and so involves orders of magnitude which are small relative to those which have figured in the current discussions.

1. *The impact on Treasury interest costs*

The two methods for expanding the money supply which are considered here do have different impacts on Treasury interest costs. Moreover, the nature of the differential impact is clear enough; Treasury borrowing costs will be smaller if the money supply is expanded through an enlargement of System holdings of Treasury securities. This is partly because the percentage of income returned to the Treasury by the Federal Reserve is in general greater than the percentage returned in the form of taxes by private lenders. Also, if the amount of securities purchased by the Federal Reserve is large relative to the total marketable public debt, then interest rates on Treasury securities will fall relatively, with a consequent saving for the Treasury each time a portion of the public debt is refinanced.

It is very difficult to estimate even approximately the interest saving which would accrue to the Treasury if instead of lowering reserve requirements the System purchased additional Treasury securities. An extremely rough calculation suggests, however, that the saving would not be large relative to total interest payments, it would be on the order of \$15 to \$20 million per year over the next few years. Of course, one may reasonably question whether or not this is so small absolutely.

2. *The impact on bank earnings*

The two methods of expanding the money supply considered here also have different impacts on the level of member bank earnings. A reduction in reserve requirements favors member bank earnings more than an expansion of System holdings of Treasury securities. This is because under the former method the

percentage of total assets held in the form of earning assets is increased, whereas under the latter method the percentage remains unchanged.

But again, though the direction of the differential impact is clear, an exact dollar estimate of the difference is extremely difficult. Roughly, however, it would appear that if the money supply were allowed to expand 3 percent per year because of a reduction in reserve requirements, member bank net profits would be \$5 to \$10 million greater per year than if the same increase in the money supply came through an expansion of the Federal Reserve's portfolio. This differential impact represents less than 1 percent of average member bank total net profits.

3. *Interest costs versus bank earnings*

It must be stressed that the above cited estimates are very, very rough, and may be in error by as much as 50 to 100 percent. Even so, it does seem that the use of either method to expand the money supply by 3 percent per year would not alter the present picture for a good many years.¹ But this is not to say that there is not a fundamental choice involved here, for what is at the heart of the "interest costs versus bank earnings" issue is the question of what rate of return should as a matter of public policy be allowed the member banks. And this question does not have a unique economic answer.

4. *Other economic considerations*

Matters of bank earnings and interest costs aside, there are other possible contrasts in economic consequence to be considered. For example, a protracted expansion of the money supply by means of successive reductions in required reserves would eventually bring sufficiently lower reserve requirements. Some economists would regard such a development as undesirable. With total reserves, fixed, lower reserve requirements mean higher excess reserves, and a greater potential expansion of bank lending; hence the possible need for large-scale System open market operations. Other economists, however, regard this argument as fallacious; they favor low reserve requirements because of the increased leverage it gives the Federal Reserve. When required reserves are small relative to deposits, small-scale open-market operations, which carry little danger of disorganizing the market for Treasury securities, have a more pronounced impact on member banks' lending power.

On the other hand, continued expansion of the Federal Reserve's holdings of Treasury securities means a steady withdrawal from the open market of a type of security which certain classes of lenders value highly because of its liquidity and risklessness. Thus, increasing the money supply by this means could force changes in long-standing portfolio-management practices. Again, however, some economists would minimize the significance of this possibility by pointing to the rapid growth of Government-guaranteed debt claims.

JULY 28, 1959.

To: Senator Paul H. Douglas, chairman.

From: John Kareken.

Subject: Calculating the impact of Federal Reserve purchases of Treasury securities on Treasury interest costs.

1. The procedure underlying the calculation presented in the original memorandum can be stated in a general way: (a) An assumption is made about the desired rate of growth of the money supply; (b) this assumption, when worked through the mechanics of the aggregate balance sheet for all commercial banks, gives a figure for the necessary Federal Reserve securities purchases; (c) then this latter figure is multiplied by the average interest rate on Treasury debt outstanding; (d) next, the gross interest figure derived in (c) is multiplied by the percent of gross income which the Federal Reserve returns to the Treasury; (e) then the gross interest figure is multiplied by the percent of gross income

¹ Once again it must be emphasized that the estimates cited here pertain to long-run, and therefore gradual, changes in the money supply. Thus, the fact that interest cost savings and increases in bank earnings appear relatively small may not contradict the views of Representatives Patman and Reuss and those of Professor Hansen (see H. Rept. No. 403, on "Member Bnk Reserve Requirements," report of the Committee on Banking and Currency on S. 1120, 86th Cong., 1st sess., May 28, 1959); they were concerned with different orders of magnitude. Also, the smallness of these estimates may in no way conflict with the view that the Treasury would have benefited considerably if instead of reducing required reserves over the postwar period the Federal Reserve had expanded the money supply equivalently by purchasing Treasury securities.

which the member banks return to the Treasury in the form of taxes; (f) finally, subtracting the figure obtained in (e) from that obtained in (d) gives the saving of the Treasury.

2. In what follows, the exact calculations are reproduced:

(a) It is assumed that the money supply should grow at the rate of 3 percent per year. Thus, since the initial net demand deposit figure is \$105 billion, net demand deposits must increase \$3.15 billion. And, since the initial publicly held currency figure is \$29 million, publicly held currency must increase \$0.9 million in the first year.

(b) Taking the current reserve requirements for the three types of member banks and weighting these by the respective total deposit figures gives an overall reserve requirement of 15 percent. Hence, the deposit-expansion multiplier is 6.667.

(c) The mechanics of the consolidated balance sheet for all member banks are such that the growth figures stated in 2(a) above require that the Federal Reserve purchase roughly \$0.473 billion of Treasury securities in the first year.¹

(d) It is assumed that the Federal Reserve returns 71 percent of gross income to the Treasury, and that the member banks return 14 percent of gross income in the form of taxes. Hence, if securities are switched from the member banks to the Federal Reserve, the Treasury realizes a saving of 57 percent in interest payments.

(e) It is assumed that the average interest rate on outstanding marketable Treasury debt is 2.8 percent per year. Thus, the gross interest on the Federal Reserve first-year purchase is \$13.2 million.

(f) Now, since the differential accruing to the Treasury is 57 percent, we get a Treasury saving of \$7.5 million.

(g) As the attached table shows, Treasury savings would be more than double in the second year. It saves \$7.8 million on Federal Reserve purchases in the second year. But it also saves \$7.5 million in the second year on Federal Reserve purchases made in the first year, thus giving a total figure for the second year of \$15.3 million.

(h) As the attached table also shows, average saving per year for the first 4 years would be \$19.4 million.

(i) The average saving per year for the first 10 years would be \$45.4 million, with savings in the 10th year in excess of \$80 billion.

(j) As was indicated in the original memo, these are very rough calculations, and are necessarily arbitrary in some degree. It is believed that they give the correct orders of magnitude. But different assumptions, which could reasonably be made, could produce somewhat different results.

	Yearly increase in net demand deposits ¹	Yearly increase in publicly held currency ²	Yearly Federal Reserve securities purchases	Interest cost on Federal Reserve securities purchases ³	Yearly interest saving for Treasury ⁴
	<i>Billion</i>	<i>Billion</i>	<i>Billion</i>	<i>Billion</i>	<i>Million</i>
1st year.....	\$3.15	\$0.0009	\$0.473	\$13.2	\$7.5
2d year.....	3.24	.0009	.486	13.6	15.3
3d year.....	3.34	.0009	.501	14.0	23.3
4th year.....	3.44	.0010	.516	14.4	31.5
5th year.....	3.55	.0010	.533	14.9	40.0
6th year.....	3.65	.0010	.548	15.3	48.7
7th year.....	3.76	.0010	.564	15.8	57.7
8th year.....	3.87	.0011	.581	16.3	67.0
9th year.....	3.99	.0011	.599	16.8	76.6
10th year.....	4.11	.0011	.617	17.3	86.5
Total.....					454.1
Average.....					45.4

¹ The initial figure used for net demand deposits was \$105,000,000,000.

² The initial figure used for publicly held currency was \$29,000,000.

³ The assumed interest rate was 2.8 percent per year.

⁴ It was assumed that the Federal Reserve returns 71 percent of gross income to the Treasury, and that the commercial banks return 14 percent.

¹ It is assumed here that this entire amount is purchased from the member banks. Alternative assumptions do not materially influence the results presented below.

JULY 28, 1959.

MEMORANDUM

To: Senator Paul H. Douglas, Chairman.

From: John Kareken.

Subject: Calculating the impact on bank profits of reductions in reserve requirements and Federal Reserve purchases of Treasury securities.

1. First we calculate what the increase in bank profits would be if a provision for a 3 percent per year growth in net demand deposits were made possible by successive reductions in reserve requirements. Then we calculate what the increase in bank profits would be if provision for the same growth were made by the transfer of Treasury securities from the commercial banks to the Federal Reserve. Comparing these calculations, we thus get a measure of the differential impact on bank profits.

2. It is assumed, then, that net demand deposits are to grow at the rate of 3 percent per year.¹ The initial net demand deposit figure is assumed to be \$105 billion, so that the deposit growth in the first year will be \$3.15 billion.

3. The required increase in excess reserves (x), and the new average reserve requirement (R), assuming we start from an initial reserve requirement of 15 percent, are given by:

$$\begin{aligned} (D)(R) &= 15.75 - x \\ x &= (d)(R) \end{aligned}$$

where D is total net demand deposits, and d is the change in D. For D=105 and d=3.15, we get:

$$\begin{aligned} R &= 14.56 \text{ percent} \\ x &= \$0.4586 \text{ billion} \end{aligned}$$

That is, reducing reserve requirements from 15 to 14.56 percent and thereby creating \$0.4486 billion of excess reserves, will allow an expansion of loans² and net demand deposits of \$3.15 billion.

4. Thus, since the ratio of net (after tax) profits to total loans is assumed to be 0.009,³ this increase in loans means an increase in net profits of \$28.35 million.

5. But, of course, if net demand deposits are expanded through Federal Reserve purchases of Treasury securities, loans will also increase, and by exactly the same amount, i.e., \$3.15 billion. In this case, however, member bank holdings of Treasury securities will decline by the amount of Federal Reserve purchases (\$0.472 billion).⁴ Thus, total net profits will be lower by this amount multiplied by the ratio of net profits on Treasury securities to total holdings of Treasury securities, which is assumed to be 0.007; that is, total net profits are lower by \$3.3 million.

6. This figure of \$3.3 million is therefore the amount that member bank net profits will increase over and above what they will be if the 3 percent expansion of the money supply is accomplished by Federal Reserve purchases of securities.

7. As the attached table shows, the differential gain in profits will be more than double in the second year. For, if reserve requirements are reduced again, this time to 13.74 percent, member banks will gain relatively not only because they do not have to give up Treasury securities in the second year, but also because they did not have to give up Treasury securities in the first year.

8. As the attached table also shows, the average differential gain in net profits over the first 10 years, using the 0.007 figure, is \$19.86 million, or about 1.5 percent of 1957-58 average net profits. If the 0.014 figure is used, average net profit over the first 10 years is \$39.72 million or roughly 3 percent of the 1957-58 average.

¹ Because it is so small relatively, the 3 percent per year increase in publicly held currency is ignored in the calculations.

² It is assumed that the increase in earning assets is in loans or in investments other than Treasury securities. For the sake of brevity, both categories are referred to as loans.

³ No statistics are readily available on the ratio of net profits on loans to total holdings of loans. The average ratio for 1957 and 1958 of net profits to total assets, as given by the Federal Reserve, is 0.0071. Thus, on the assumption that Treasury securities yield less than other noncash earning assets, the needed ratio is assumed to be 0.009. Also, it is assumed that the ratio of net profits on Treasury securities to total Treasury securities held is 0.007. Both of these assumptions probably have the result of understating net profits. Indeed, if it is assumed that the cost (other than tax payments) of managing an increment to the commercial banks' holdings of Treasury securities is zero, then the ratio of net (after tax) profits to total holdings of Treasury securities would be roughly 0.014. Changing this ratio from 0.007 to 0.014 would have the effect of doubling the net profit figures given on the attached table.

⁴ See the table in the accompanying memorandum.

9. Again, however, it should be emphasized that the above calculations are necessarily arbitrary in some degree. It is believed that they give the correct orders of magnitude, but different assumptions, which could reasonably be made, could produce somewhat different results.

	New reserve requirements ¹	Yearly increase in earning assets ²	Yearly differential increase in member bank net profits ³	
			0.007 ⁴	0.014 ⁴
	<i>Percent</i>	<i>Billion</i>	<i>Million</i>	<i>Million</i>
1st year.....	14.56	\$3.15	\$3.3	\$6.6
2d year.....	14.14	3.24	6.7	13.4
3d year.....	13.73	3.34	10.2	20.4
4th year.....	13.33	3.44	13.8	27.6
5th year.....	12.94	3.55	17.5	35.0
6th year.....	12.56	3.65	21.3	42.6
7th year.....	12.20	3.76	25.2	50.4
8th year.....	11.84	3.87	29.3	58.6
9th year.....	11.50	3.99	33.5	67.0
10th year.....	11.16	4.11	37.8	75.6
Total.....			198.6	397.2
Average.....			19.86	39.72

¹ Reserve requirements were assumed to be 15 percent initially.

² It was assumed that all increases in excess reserves, created by the reductions in reserve requirements, were put into loans and investments other than Treasury securities.

³ This is the gain in net profits over and above the increase which would have resulted if the Federal Reserve had purchased Treasury securities to expand the money supply.

⁴ The figures appearing here are approximate ratios of net profits on holdings of Treasury securities to total holdings of Treasury securities. The 0.007 figure is an average ratio, and thus makes allowance for expenses other than taxes. The 0.014 figure assumes that the only expenses are taxes.

JULY 20, 1959.

To: Members of the Joint Economic Committee.

From: Otto Eckstein and John H. Kareken.

Subject: Interest rate ceiling.

I. BACKGROUND

It is presently impossible for the Treasury to sell long-term Government securities below the legal interest rate ceiling. Long-term interest rates have been rising for the last 10 years. The rate on Government securities has been rising particularly because of the growth of competition for low-risk long-term funds. The present high levels, which have occurred extraordinarily early in the recovery from the last recession, are partly due to the speculative collapse of the Government bond market last summer and the continued subsequent decline. Monetary policy has been tighter earlier in this recession than in the last one, a policy based on the widely held belief that monetary policy had been too loose at the bottom of the 1954 recession, had been tightened too slowly and had thereby set the stage for the subsequent inflation.

II. THE CASE FOR ABOLISHING THE INTEREST CEILING

1. The ceiling is arbitrary, just like the debt limit, and economic policy is not formulated wisely by fighting over such peculiar rules.

2. If the national debt is to be managed in a neutral manner, the average maturity cannot be allowed to fall steadily, for this increases the amount of short-term securities and decreases the Government's share of long-term securities. This shortening of the debt goes on all the time, independent of the specific maturity dates of old long-term issues. While this definition of neutrality is arbitrary, it is true that selling no long-terms whatsoever over a substantial period of time has a net inflationary effect. It releases funds tied up in long-term Government securities to finance new private long-term investments.

3. In the event inflation develops, and assuming that it is partly caused by excess long-term investment, the Treasury should sell long-term securities. It is true that there are few inflationary pressures now visible in the economy and that little of them can be blamed on long-term investment. But to preserve the Treasury's capability to sell long-term bonds is a kind of insurance.

4. It is likely that sooner or later the interest ceiling will have to be raised since there are genuine long-run forces that work in the economy serving to raise interest rates. This may be as good a time as any to dispose of the issue and future Secretaries of the Treasury may be grateful.

5. European financial circles are supposed to be concerned about American inflation, and failure to raise interest rates may lead to speculative movements of capital from the United States to Europe. This would accentuate the gold drain.

6. If the Treasury issues no long-terms, it has to issue more short-terms which are turned over so frequently. This complicates debt management and monetary policy in the future.

III. THE CASE AGAINST ABOLISHING THE INTEREST CEILING

1. While the interest ceiling is arbitrary, the occurrence of the statutory bottlenecks does provide the Congress with one of the few opportunities to question monetary policies.

2. The rise in the ceiling will permit the Federal Reserve and the administration to continue their economic policies in exactly the same form as they have been doing. Thus the debate about the interest ceiling should consider the wisdom of present policies.

3. Issuance of new long-term bonds as part of anti-inflation policy inevitably will take long-term funds away from somebody else; just as past monetary policy has primarily affected mortgages, and secondarily, State and local governments, public utilities, and small businesses, so a long-term issue of Treasury securities may have the same specific sectoral impact.

4. The bills-only doctrine of the Federal Reserve System (by which the Federal System ordinarily limits itself to purchases and sales of short-term bills) is one of the contributory causes for the present high level of interest rates but this is mostly crying about spilled milk. Abandonment of bills-only now would nevertheless help in the future.

5. Given the several causes of inflation, i.e., specific excess demands in certain industries, the independent power of management and labor in monopolistic markets to raise their prices, and perhaps some general excess demand, a policy of higher interest rates will not solve the problems entirely.

6. Such an unbalanced program to fight inflation, i.e., a program of tightening long-term credit without complementary fiscal and monetary measures, will have adverse effects on economic growth.

IV. ARE THERE ALTERNATIVES?

Given the many inflationary hazards in our economy, it is not a safe policy to gamble on stable prices for the period from now until the Congress meets again. There must be an arsenal of anti-inflationary weapons. Besides moral suasion, the Government currently can do little except engage in open-market policy to affect bank loans with a gradual spillover to the long-term capital market. Treasury issue of long-term bonds widens the arsenal somewhat, permitting the Treasury to affect the availability of long-term money. This is a substitute for Federal Reserve action in the long-term market.

The wisdom of this set of policies (open-market policy on short-term plus a possible long-term Treasury issue) can be questioned and broader policy packages can be devised. If sufficient alternatives are employed, a more effective anti-inflationary policy can be pursued, and incidentally, the need to raise long-term interest rates can be obviated. We list some of the possible alternative policies that could be explored:

(a) *Money and credit policies*

1. Abandonment of bills—only doctrine, permitting the Federal Reserve to sell long-term issues if anti-inflation policy requires it. This very likely would make the need for getting rid of the interest ceiling even greater next year.

2. Tighten the terms of mortgages. This would serve to restore the position of Treasury securities in relation to the competition which the Government has created for itself by guaranteeing mortgages.

3. Regulate consumer credit. This could make the impact of anti-inflation policies at least partly fall on consumption, thereby raising the rate of growth of the economy. It would also get at one of the sources for instability.

(b) *Fiscal policies*

1. Revenues could be increased by closing loopholes or perhaps even by more general measures such as increases in the rates.
2. Depreciation allowances could be made variable.
3. Certain expenditure programs could be cut back in inflation such as highways, water resource projects, and other public works.

(c) *Market structure policies*

1. If inflation is caused by concentration of market power to any significant extent, none of the above policies will be wholly effective. There might be some exploration of policies dealing with this problem.

(d) *Reduce the direct inflationary impact of Government*

1. Convert the agriculture price support program into some other form.
2. Reduce tariffs, quotas, and "buy American" provisions.
3. Use more income taxes and less excise and property taxes, especially at State levels, since the latter gets into the Consumer Price Index. This would require greater assumption of fiscal responsibility by Federal Government.

JULY 20, 1959.

To: Members of the Joint Economic Committee.

From: Otto Eckstein and John Kareken.

Subject: A background memo on the use of the auction technique for marketing Treasury securities.

A. INTRODUCTION

At present the Treasury uses different marketing techniques for selling bills and for selling certificates of indebtedness, notes and bonds. Bills are sold by the auction, or sealed-bid technique, which can be briefly described as follows: the Treasury makes known the maturity of the bills to be issued, then receives sealed bids from interested lenders, and then makes allocations according to the bids received. Certificates, notes and bonds are marketed differently; the Treasury announces all the terms of the contract and then opens its subscription book for orders at the announced terms. Thus, in the former case the bids of the private market, when matched against the quantity of funds the Treasury needs, determines the price of the new issue of bills. In the latter case, the price is announced by the Treasury, and the quantity of securities sold is determined by the orders given to the Treasury on the basis of the quoted price.

Currently, there has been a good deal of debate about whether or not the Treasury should market all of its securities—bonds as well as bills—by means of the auction technique.

B. THE CASE FOR GREATER UTILIZATION OF THE AUCTION TECHNIQUE

Essentially, there are two basic arguments advanced in support of greater utilization of the auction technique in the marketing of certificates, notes and bonds. The first, and most important, has to do with the influence of Treasury debt operations on the activities of the Federal Reserve. The second relates to the possibility that the present technique for marketing certificates, notes and bonds may involve the payment of unnecessarily high interest rates because it does involve an attempt to guess ahead of time what the price of the new issue should be.

1. It is often argued that the Federal Reserve is effectively blocked from changing the degree of monetary restraint for 2 or 3 weeks before and after a Treasury financing operation. Why? Because under present arrangements the Treasury announces beforehand the price at which its securities are to be sold. Thus, any move by the System to change interest rates might doom the Treasury issue to failure. Moreover, this kind of limitation on the Federal Reserve's freedom of action becomes serious when the Treasury has to be in the market several times a year with nonbill financings. If, however, the Treasury were to auction its bonds, notes and certificates, as well as its bills, the Federal Reserve would have to be less concerned that any actions it took would spoil the Treasury's market.

2. When securities are offered by the Treasury according to its guess as to what their price should be, there is the chance that the quoted interest rate will be too high and so will involve a subsidy to private lenders. This appearance

is even harder to avoid when the Treasury, by long-standing practice, makes use of advisory groups drawn from the financial community in marketing its bonds and notes. Admittedly, it is very difficult to determine whether or not subsidies are actually paid by the Treasury. (For one thing, it must be expected that the Treasury will typically have to pay something in the form of a marketing fee to those who purchase the new securities for distribution to permanent investors.) But the auction technique would tend to rid the marketing process of the possibility of the sort of subsidy which could be present under present marketing arrangement.

C. THE CASE AGAINST GREATER UTILIZATION OF THE AUCTION TECHNIQUE

It is not an easy thing to produce arguments against the greater utilization of the auction technique in the marketing of Treasury bonds, notes and certificates. This is not to say that there may not be such arguments. Rather, it is meant only to suggest that the Treasury should be asked to make a case against the auction technique if, as it appears, the Treasury does not choose to make use of this method.

It is possible to cite one argument advanced against the auction technique, namely, that private investors are not familiar enough with this method. This may be so, but if the auction technique is superior to the present method, then it is worth some expenditure of money by the Treasury to educate these investors. That is to say, one should be interested in the net gain to be had from switching to the auction technique.

JULY 21, 1959.

To: Members of the Joint Economic Committee.

From: Otto Eckstein and John Kareken.

Subject: A background memo on the market for Government securities.

The following brief remarks are intended only to summarize some of the more important developments in the market for Treasury securities. These developments are covered in detail in the attached materials.

A. THE ABSOLUTE AND RELATIVE IMPORTANCE OF TREASURY DEBT

The attached tables shows, among other things, that—

1. total public (Federal) debt has increased little in the past few years; in April 1958 the total was only 111.8 percent of the mid-1951 total;
2. total public debt has been declining in importance relative to total debt in the postwar period; in 1945 it was about 60 percent of total debt, but at the end of 1958 it was only slightly more than 31 percent;
3. marketable debt has been increasing in importance relative to total debt; in mid-1951 it was 54.5 percent of total debt, and at the end of March 1959 was 62.9 percent;
4. that Federal agency issues not guaranteed by the Treasury, while becoming more important, still do not loom very large in the total Federal debt picture; in mid-1953 these securities totalled roughly \$2.1 billion or 1.4 percent of total marketable debt, whereas in March 1959 they totalled \$5.9 billion or 3.3 percent of total marketable debt;
5. savings bonds have been decreasing in importance relative to total public debt (series E savings bonds, not shown separately in the attached tables, have increased slightly in dollar amount: From \$34.7 billion at the end of 1951 to \$38.2 billion at the end of 1958).

B. THE MATURITY LENGTH OF THE PUBLIC DEBT

1. The attached table on average debt maturity shows that except for a relatively unimportant interruption in 1954-55 the average maturity of the public debt has been on the decrease since 1949; it is interesting to note, however, that the one upturn in the average maturity figure came in a period of relatively low economic activity.

2. The following is a table of the future maturity schedule of the public debt, given by type of holder:¹

Year	Treasury investment accounts and Federal Reserve	All other investors
1959 ¹	\$13,429	\$10,566
1960.....	6,070	18,210
1961.....	3,390	17,240
1962.....	1,757	13,331
1963.....	274	13,233
1964.....	58	3,816
1965.....	595	6,301
1966.....	109	1,375
1967.....	270	1,841
1968.....	425	2,395
1969.....	1,136	7,701
1970.....	1,230	3,468
1971.....	700	2,246
1972.....	613	7,635
1974-95.....	779	7,965

¹ 1959 figure covers the period August through December.

C. INTEREST COSTS

As the attached table on interest charges shows, interest costs have been increasing since 1951; the increase in computed interest rates is most marked for the marketable component of the debt.

Other of the attached tables and charts show the current level of interest rates on Treasury guaranteed issues and on nonguaranteed agency issues.

D. PRIVATE SECTOR HOLDINGS OF TREASURY SECURITIES

As the appropriate charts taken from the Federal Reserve chart books which are included here show—

1. *For commercial banks.*—On trend, commercial banks' dollar holdings of Treasury securities have declined since the end of World War II; more importantly, these holdings have fluctuated sharply, increasing in periods of recession and decreasing in periods of prosperity.

2. *For savings institutions.*—Life insurance companies' dollar holdings of Treasury securities have declined steadily since the end of World War II; similarly, mutual savings banks' dollar holdings have also declined steadily, though less sharply; and, since total assets of life insurance companies and mutual savings banks have gone up over the same period, the relative importance of Treasury securities in the respective aggregate portfolios has declined even more sharply than dollar holdings. For savings and loan associations, on the other hand, total dollar holdings of Treasury securities have risen steadily but slowly over the postwar years; again, however, Treasury securities have declined in relative importance.

3. *For other investors.*—This class of investors, which includes individuals and nonfinancial corporations, State and local governments, pension funds, trusts, etc., shows an increase in its holdings of Treasury securities for the postwar period.

¹ Figures taken from Treasury Bulletin, June 1959, and are given as millions of dollars.

DEBT OUTSTANDING
TABLE 1—Summary of Federal securities
[In millions of dollars]

End of fiscal year or month	Total outstanding			Interest-bearing debt			Matured debt and debt bearing no interest					
	Total ¹	Public debt	Guaranteed securities ²	Total	Public debt	Guaranteed securities ² ³	Total	Public debt				Guaranteed securities ² (matured)
								Total	Matured	Monetary fund ⁴	Other ⁵	
1951.....	255,251	255,222	29	252,879	252,852	27	2,372	2,370	512	1,283	575	2
1952.....	259,151	259,105	46	256,907	256,863	44	2,244	2,242	410	1,274	550	1
1953.....	266,123	266,071	52	263,997	263,946	51	2,126	2,125	298	1,302	525	1
1954.....	271,341	271,260	81	268,990	268,910	80	2,351	2,350	437	1,411	502	1
1955.....	274,418	274,374	44	271,785	271,741	43	2,634	2,633	589	1,567	477	1
1956.....	272,825	272,751	74	269,956	269,883	73	2,869	2,868	666	1,742	460	1
1957.....	270,634	270,527	107	268,592	268,486	106	2,042	2,042	529	1,068	444	1
1958.....	276,444	276,343	101	274,798	274,698	101	1,646	1,646	597	618	430	1
1957—December.....	275,002	274,898	104	272,977	272,874	104	2,025	2,024	841	746	437	1
1958—July.....	275,568	275,466	102	274,011	273,910	101	1,557	1,556	497	632	427	1
August.....	278,584	278,476	108	277,058	276,951	108	1,526	1,525	481	619	425	1
September.....	276,784	276,666	118	275,122	275,004	117	1,662	1,661	611	626	424	1
October.....	280,323	280,211	112	278,672	278,561	111	1,651	1,650	541	687	423	1
November.....	283,167	283,060	107	281,531	281,425	106	1,636	1,635	524	687	424	1
December.....	283,031	282,922	109	280,947	280,839	108	2,084	2,084	903	757	423	1
1959—January.....	285,907	285,801	106	283,913	283,808	105	1,994	1,993	822	745	422	1
February.....	285,216	285,104	112	283,354	283,243	111	1,861	1,861	677	762	422	1
March.....	282,153	282,034	119	280,207	280,089	118	1,946	1,945	603	923	419	1
April.....	285,460	285,353	107	283,603	283,497	106	1,856	1,856	518	919	419	1

¹ Includes certain obligations not subject to statutory limitation. For amounts subject to limitation, see p. 1.

² Excludes guaranteed securities held by the Treasury.

³ Consists of Federal Housing Administration debentures beginning March 1953.

⁴ Special notes of the United States issued to the International Monetary Fund in payment of part of the U.S. subscription pursuant to provisions of the Bretton Woods

Agreements Act. The notes bear no interest, are nonnegotiable, and are payable on demand.

⁵ Includes savings stamps, excess profits tax refund bonds, and currency items. For current month detail, see "Statutory Debt Limitation," table 2.

Source: Daily Treasury statement.

TABLE 2.—Computed interest charge and computed interest rate on Federal securities

[Dollar amounts in millions]

End of fiscal year or month	Total interest-bearing securities				Total interest-bearing securities	Computed annual interest rate									
	Amount outstanding		Computed annual interest charge			Total public debt	Public debt								Guaranteed securities ¹
	Public debt and guaranteed securities ¹	Public debt	Public debt and guaranteed securities ¹	Public debt			Marketable issues					Non-marketable issues ⁴	Special issues		
							Total ²	Bills ³	Certificates	Notes	Treasury bonds				
1951.....	252,879	252,852	5,740	5,740	2,270	2,270	1,981	1,569	1,875	1,399	2,327	2,623	2,606	2,656	
1952.....	256,907	256,863	5,982	5,981	2,329	2,329	2,051	1,711	1,875	1,500	2,317	2,659	2,675	2,578	
1953.....	263,997	263,946	6,432	6,431	2,438	2,438	2,207	2,254	2,319	1,754	2,342	2,720	2,746	2,575	
1954.....	268,990	268,910	6,300	6,298	2,342	2,342	2,043	.843	1,928	1,838	2,440	2,751	2,671	2,547	
1955.....	271,785	271,741	6,388	6,387	2,351	2,351	2,079	1,539	1,173	1,846	2,480	2,789	2,585	2,590	
1956.....	269,956	269,883	6,952	6,950	2,576	2,576	2,427	2,654	2,625	2,075	2,485	2,824	2,705	2,606	
1957.....	268,592	268,486	7,328	7,325	2,730	2,730	2,707	3,197	3,345	2,504	2,582	2,853	2,635	2,611	
1958.....	274,798	274,698	7,248	7,245	2,638	2,638	2,546	1,033	3,330	2,806	2,576	2,892	2,630	2,622	
1957—December.....	272,977	272,874	7,878	7,876	2,889	2,889	2,965	3,610	3,699	2,866	2,505	2,875	2,639	2,619	
1958—July.....	274,011	273,910	7,210	7,208	2,632	2,632	2,534	.951	3,329	2,801	2,575	2,895	2,633	2,627	
August.....	277,058	276,951	7,019	7,016	2,534	2,534	2,374	1,185	2,361	2,790	2,585	2,897	2,635	2,625	
September.....	275,122	275,004	7,088	7,085	2,577	2,577	2,443	1,702	2,361	2,785	2,592	2,899	2,637	2,629	
October.....	278,672	278,561	7,370	7,367	2,647	2,647	2,558	2,512	2,361	2,823	2,592	2,902	2,640	2,638	
November.....	281,531	281,425	7,536	7,533	2,679	2,679	2,610	2,836	2,361	2,823	2,592	2,904	2,643	2,623	
December.....	280,947	280,839	7,546	7,543	2,689	2,689	2,624	2,930	2,212	2,954	2,592	2,909	2,646	2,621	
1959—January.....	283,913	283,808	7,670	7,667	2,704	2,704	2,649	2,960	2,212	2,995	2,607	2,912	2,648	2,620	
February.....	283,354	283,243	7,871	7,868	2,751	2,751	2,769	2,995	2,599	3,276	2,608	2,915	2,650	2,618	
March.....	280,207	280,089	7,839	7,836	2,801	2,801	2,799	3,020	2,713	3,266	2,608	2,918	2,653	2,612	
April.....	283,603	283,497	7,995	7,993	2,824	2,824	2,832	3,101	2,713	3,311	2,619	2,921	2,656	2,622	

¹ Excludes guaranteed securities held by the Treasury.

² Total includes "Other bonds"; see table 3.

³ Included in debt outstanding at face amount, but discount value is used in computing annual interest charge and annual interest rate.

⁴ The annual interest charge and annual interest rate on U.S. savings bonds are computed on the basis of the rate to maturity applied against the amount outstanding.

NOTE.—The computed annual interest charge represents the amount of interest that would be paid if each interest-bearing issue outstanding at the end of each month or year

should remain outstanding for a year at the applicable annual rate of interest. The charge is computed for each issue by applying the appropriate annual interest rate to the amount outstanding on that date. The aggregate charge for all interest-bearing issues constitutes the total computed annual interest charge. The average annual interest rate is computed by dividing the computed annual interest charge for the total, or for any group of issues, by the corresponding principal amount.

Source: Daily Treasury statement.

TABLE 3.—Interest-bearing public debt

[In millions of dollars]

End of fiscal year or month	Total interest-bearing public debt	Public issues													Special issues	
		Total public issues	Marketable						Nonmarketable							
			Total	Bills	Certificates	Notes	Treasury bonds		Other bonds ²	Total	U.S. savings bonds	Treasury savings notes	Armed Forces leave bonds	Treasury bonds, investment series		Depository bonds
							Bank eligible	Bank restricted ¹								
1951.....	252,852	218,198	137,917	13,614	9,509	35,806	42,772	36,061	156	80,281	57,572	7,818	47	14,526	319	34,653
1952.....	256,863	219,124	140,407	17,219	28,423	18,963	48,200	27,460	142	78,717	57,685	6,612	-----	14,046	373	37,739
1953.....	263,946	223,408	147,335	19,707	15,854	30,425	63,980	17,245	124	76,073	57,836	4,453	-----	13,288	447	40,538
1954.....	268,910	226,681	150,354	19,515	18,405	31,960	71,706	8,672	96	76,326	58,061	5,079	-----	12,775	411	42,229
1955.....	271,741	228,491	155,206	19,514	13,836	40,729	81,057	-----	71	73,285	58,365	1,913	-----	12,589	417	43,250
1956.....	269,883	224,769	154,953	20,808	16,303	35,952	81,840	-----	50	69,817	57,497	-----	-----	12,000	310	45,114
1957.....	268,486	221,658	155,705	23,420	20,473	30,973	80,789	-----	50	65,953	54,622	-----	-----	11,135	196	46,827
1958.....	274,698	228,452	166,675	22,406	32,920	20,416	90,883	-----	50	61,777	61,984	-----	-----	9,621	171	46,246
1957—December.....	272,874	227,075	164,192	26,857	34,554	20,664	82,067	-----	50	62,883	52,474	-----	-----	10,253	156	45,799
1958—July.....	273,910	228,033	166,391	22,403	32,938	20,499	90,501	-----	50	61,642	61,913	-----	-----	9,525	204	45,877
August.....	276,951	230,638	169,233	22,401	38,487	20,665	87,631	-----	50	61,404	61,854	-----	-----	9,244	244	45,996
September.....	275,094	229,008	167,728	22,699	38,487	20,749	85,743	-----	50	61,280	61,792	-----	-----	9,109	217	45,367
October.....	278,561	233,194	172,153	25,942	38,487	21,938	85,737	-----	50	61,941	61,715	-----	-----	9,083	207	45,112
November.....	281,425	236,313	175,364	29,148	38,487	21,948	85,731	-----	50	60,949	61,680	-----	-----	9,017	203	44,840
December.....	280,839	235,999	175,586	29,748	36,364	26,072	83,352	-----	50	60,412	61,192	-----	-----	8,897	196	43,907
1959—January.....	283,808	239,901	179,816	30,342	36,364	28,918	84,142	-----	50	60,086	60,993	-----	-----	8,832	185	43,870
February.....	283,243	239,373	179,308	31,832	37,957	25,299	84,170	-----	50	60,068	61,049	-----	-----	8,692	185	43,940
March.....	280,089	236,149	176,293	32,234	34,390	25,429	84,190	-----	50	59,856	60,980	-----	-----	8,500	183	43,278
April.....	283,497	240,220	180,709	34,244	34,390	27,204	84,821	-----	50	59,510	60,819	-----	-----	-----	-----	-----

¹ Issues which commercial banks (banks accepting demand deposits) were not permitted to acquire prior to specified dates, except that (1) concurrently with the 4th, 5th, and 6th war loans and the Victory loan, they were permitted to subscribe for limited investment of their savings deposits; (2) they might temporarily acquire such issues through forfeiture of collateral; (3) they might hold a limited amount of such issues for trading purposes.

² Consists of Panama Canal bonds, and also postal savings bonds until the last of these bonds matured on July 1, 1955.

Source: Daily Treasury statement.

TABLE 4.—Average length and maturity distribution of marketable interest-bearing public debt¹

[In millions of dollars]

End of fiscal year or month	Amount outstand- ing	Maturity classes					Average length
		Within 1 year	1 to 5 years	5 to 10 years	10 to 20 years	20 years and over	
1951.....	137,917	43,908	46,526	8,707	29,979	8,797	6 years, 7 months.
1952.....	140,407	46,367	47,814	13,933	25,700	6,594	5 years, 8 months.
1953.....	147,335	65,270	36,161	15,651	28,662	1,592	5 years, 4 months.
1954.....	150,354	62,734	29,866	27,515	28,634	1,606	5 years, 6 months.
1955.....	155,206	49,703	39,107	34,253	28,613	3,530	5 years, 10 months.
1956.....	154,953	58,714	34,401	28,908	28,578	4,351	5 years, 4 months.
1957.....	155,705	71,952	40,669	12,328	26,407	4,349	4 years, 9 months.
1958.....	166,675	75,288	42,557	21,476	27,652	7,208	5 years, 3 months.
1957—December.....	164,192	47,995	47,995	8,868	27,690	4,347	4 years, 7 months.
1958—July.....	166,391	67,797	42,639	21,101	27,647	7,208	5 years, 2 months.
August.....	169,233	70,477	49,559	14,347	27,642	7,208	5 years, 1 month.
September.....	167,728.	68,896	49,643	14,347	27,633	7,207	5 years, 1 month.
October.....	172,153	72,117	50,854	14,347	27,627	7,207	4 years, 11 months.
November.....	175,364	76,506	49,195	15,832	27,623	7,207	4 years, 9 months.
December.....	175,586	72,616	53,803	17,167	24,793	7,206	4 years, 9 months.
1959—January.....	179,816	73,210	56,650	17,167	24,786	8,004	4 years, 9 months.
February.....	179,308	71,191	61,986	13,312	24,779	8,039	4 years, 9 months.
March.....	176,293	68,025	62,117	13,312	24,771	8,068	4 years, 9 months.
April.....	180,709	70,115	63,811	13,311	25,383	8,089	4 years, 8 months.

Source: Office of the Secretary, Debt Analysis Staff.

¹ All issues classified to final maturity except partially tax-exempt bonds which are classified to earliest call date.

TREASURY SURVEY OF OWNERSHIP, MAR. 31, 1959

SECTION II.—Interest-bearing securities issued by Federal agencies but not guaranteed by the U.S. Government

[Par values—in millions of dollars]

Issue (Tax status is shown in parentheses)	Total amount outstanding ¹	Held by investors covered in Treasury survey				Held by all other investors	Memo-randum: Held by 10,484 corporate pension trust funds	
		6,450 commercial banks	516 mutual savings banks	Insurance companies				U.S. Government investment accounts and Federal Reserve banks
				304 life	539 fire, casualty, and marine			
Banks for cooperatives:								
2.85 percent April 1959 (Debentures) (taxable).....	82	25	7	(*)	1	50	(*)	
3½ percent June 1959 (Debentures) (taxable).....	98	24	8	(*)	1	64	(*)	
3.55 percent August 1959 (Debentures) (taxable).....	78	14	3	(*)		62	(*)	
Total banks for cooperative securities.....	258	62	17	(*)	2	176	1	
Federal home loan banks: ²								
3½ percent April 1959 (Notes) (taxable).....	106	22	7		1	76	(*)	
3½ percent August 1959 (Notes) (taxable).....	222	35	11	5	1	170	3	
3½ percent September 1959 (Notes) (taxable).....	96	24	2	(*)	1	69	4	
3½ percent April 1963 (Bonds) (taxable).....	275	89	11	1	4	170	(*)	
Total Federal home loan bank securities.....	699	170	31	6	7	485	7	
Federal intermediate credit banks:								
Debentures (taxable).....	1,206	304	58	15	17	813	7	
Federal land banks: ³								
2¼ percent May 1959 (Bonds) (taxable).....	71	30	6	(*)	1	33	1	
3½ percent May 1959 (Bonds) (taxable).....	120	34	9	(*)	1	76	1	
1¾ percent October 1959 (Bonds) (taxable).....	164	70	5		2	87	1	
2¼ percent February 1960 (Bonds) (taxable).....	124	68	1	(*)	2	52	1	
3¾ percent February 1960 (Bonds) (taxable).....	89	26	4	(*)	2	57	(*)	
2¼ percent June 1960 (Bonds) (taxable).....	106	49	6	(*)	3	49	1	
3¾ percent April 1961 (Bonds) (taxable).....	83	35	6		2	39	1	
4 percent September 1961 (Bonds) (taxable).....	120	39	5	(*)	2	74	3	
4 percent May 1962 (Bonds) (taxable).....	125	20	5		1	98	5	
2¾ percent May 1963 (bonds) (taxable).....	122	72	6		1	42	2	
3¼ percent May 1966 (bonds) (taxable).....	108	39	11	(*)	4	54	3	
4½ percent February 1967-72 (bonds) (taxable).....	72	2	5		1	58	12	
4½ percent October 1967-70 (bonds) (taxable).....	75	4	10		1	56	8	

4½ percent March 1969 (bonds) (taxable).....	100	11	11	3	4	71	11
4½ percent July 1969 (bonds) (taxable).....	60	2	7	1	1	48	8
3½ percent April 1970 (bonds) (taxable).....	83	9	9	1	1	64	5
3½ percent May 1971 (bonds) (taxable).....	60	(*)	6	3	2	49	11
3½ percent September 1972 (bonds) (taxable).....	109	(*)	5	5	3	95	21
Total Federal land bank securities.....	1,792	512	116	24	36	1,103	40
Federal National Mortgage Association:							
1.65 percent April 1959 (debentures) (taxable).....	100	29	5	(*)	1	65	(*)
2 percent June 1959 (debentures) (taxable).....	100	26	4	1	1	68	(*)
3½ percent August 1959 (debentures) (taxable).....	100	22	4	(*)	2	72	1
3½ percent October 1959 (debentures) (taxable).....	100	19	5	1	2	73	(*)
4 percent June 1960 (debentures) (taxable).....	100	20	3	(*)	7	70	(*)
3½ percent August 1960 (notes) (taxable).....	797	397	55	2	16	325	4
3½ percent February 1962 (debentures) (taxable).....	200	55	24	1	6	113	7
3½ percent March 1963 (debentures) (taxable).....	150	53	17	(*)	4	76	3
4½ percent November 1963 (debentures) (taxable).....	100	21	5	1	7	65	3
4½ percent June 1965 (debentures) (taxable).....	100	24	17	1	4	54	9
3½ percent March 1968 (debentures) (taxable).....	100	15	8	1	4	72	4
Total Federal National Mortgage Association securities.....	1,947	681	147	10	54	1,052	32

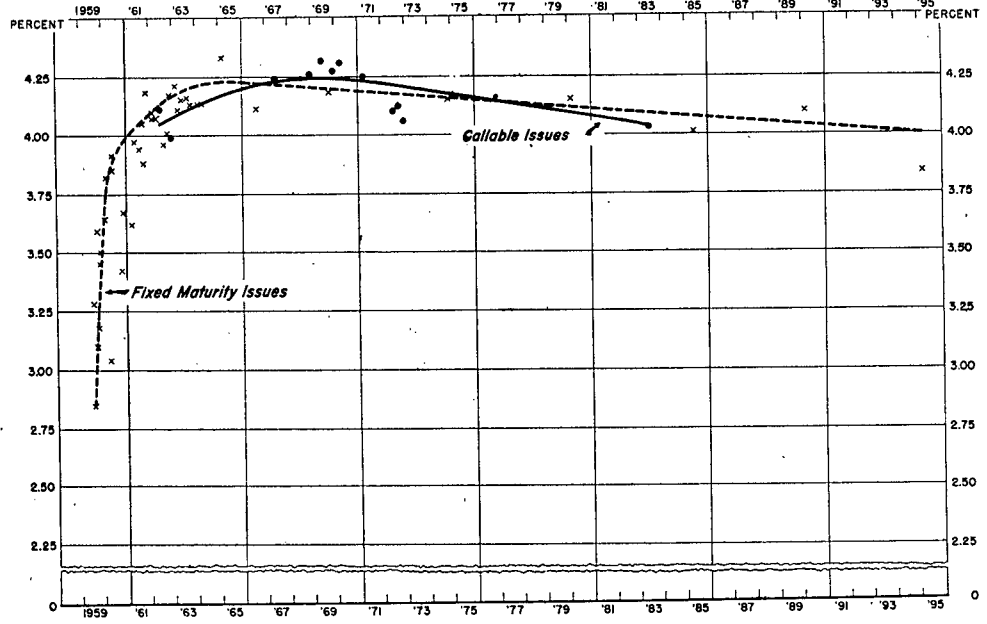
¹ Includes only publicly offered issues.

² The proprietary interest of the United States in these banks ended in July 1951.

³ The proprietary interest of the United States in these banks ended in June 1947.

*Less than \$500,000.

YIELDS OF TAXABLE TREASURY SECURITIES, APR. 30, 1959
Based on Closing Bid Quotations



Explanation: The points represent yields to call when prices are above par, and to maturity date when prices are at par or below. The smooth curves for the two classes of points are fitted by eye. Market yields on bills other than those offered the latest week and on coupon issues for which an exchange offer has been made or which are due or callable in less than 3 months are excluded.

[From the New York Times]

U.S. GOVERNMENT AND AGENCY BONDS, MONDAY, JULY 20, 1959

Bonds

Treasury	3:30 p.m.		Change in bid
	Bid	Asked	
2½s 1962-59, June.....	94.6	94.10	-----
2½s 1962-59, December.....	93.6	93.10	-----
2½s 1960, November.....	97.17	97.19	-----
2½s 1965-60, December.....	97.4	97.12	-----
¾s 1961, September.....	96.8	96.12	-----
2½s 1961, November.....	95.14	95.18	-----
2½s 1967-62, June.....	87.20	87.28	-0.4
2½s 1963, August.....	92.14	92.18	-2
2½s 1968-63, December.....	85.20	85.28	-4
3s 1964, February.....	93.24	93.28	-4
2½s 1969-64, June.....	84.22	84.30	-2
2½s 1969-64, December.....	84.8	84.16	-4
2½s 1965, February.....	90.30	91.2	-2
2½s 1970-65, March.....	84.8	84.16	-4
2½s 1971-66, March.....	84.6	84.14	-2
3s 1966, August.....	92.0	92.4	-2
2½s 1972-67, June.....	84.6	84.14	-4
2½s 1972-67, September.....	83.0	83.8	-2
2½s 1972-67, December.....	84.6	84.14	-2
4s 1969, October.....	98.6	98.14	-4
37½s 1974, November.....	96.6	96.4	-4
3½s 1983-78, June.....	87.14	87.22	-2
4s 1980, February.....	97.4	97.22	-4
3½s 1985, May.....	87.14	87.22	-----
3½s 1990, February.....	89.12	89.20	-----
3s 1995, February.....	84.18	84.26	-----

Treasury notes

Outstanding—millions	Rate	Bid	Ask	Yield
473 August 1959.....	4	100.1	100.2	1.70
99 October 1959.....	1½	99.17	99.20	3.43
1,184 November 1959.....	3½	99.30	100.0	3.48
198 April 1960.....	1½	98.22	98.28	3.15
2,406 May 1960.....	3½	99.10	99.12	2.26
2,738 May 1960.....	4½	100.0	100.1	4.70
278 October 1960.....	1½	97.16	97.22	3.50
144 April 1961.....	1½	96.0	96.8	3.81
4,078 May 1961.....	3½	98.26	98.30	4.23
2,138 August 1961.....	4	99.16	99.20	4.19
332 October 1961.....	1½	94.4	94.12	4.22
647 February 1962.....	3½	98.8	98.12	4.30
1,434 February 1962.....	4	99.8	99.12	4.26
551 April 1962.....	1½	92.26	93.2	4.26
2,000 August 1962.....	4	99.26	99.30	4.02
590 October 1962.....	1½	91.16	91.24	4.29
1,143 November 1962.....	3½	97.22	97.26	4.46
3,971 February 1963.....	2½	93.16	93.20	4.58
533 April 1963.....	1½	90.8	90.16	4.31
1,743 May 1963.....	4	98.18	98.16	4.31
506 October 1963.....	1½	88.30	89.6	4.35
137 April 1964.....	1½	87.6	87.14	4.50

Certificates of indebtedness

Outstanding—millions	Rate	Bid	Ask	Yield
13,500 August 1959.....	15%	100.0	100.1	0.49
7,711 November 1959.....	3½	99.29	99.31	3.45
11,363 February 1960.....	3½	99.22	99.24	4.18
11,363 February 1960.....	3¾	99.23	99.25	4.14
1,269 May 1960.....	4	99.24	99.28	4.14

Federal Intermediate Credit Bank debentures

Outstanding—millions	Rate	Bid	Ask	Yield
133 August 1959.....	3.60	100.0	100.1	2.59
124 September 1959.....	3½	100.0	100.1	3.15
178 October 1959.....	3.45	99.29	99.31	3.54
187 November 1959.....	3.45	99.28	99.30	3.62
196 December 1959.....	3.70	99.27	99.30	3.82
190 January 1960.....	3¾	99.23	99.27	4.05
181 February 1960.....	4½	99.22	99.25	4.51
171 March 1960.....	4½	99.26	99.29	4.63
160 April 1960.....	4.45	99.25	99.28	4.62

Federal Home Loan Bank

Outstanding—millions	Rate	Bid	Ask	Yield
222 August 17, 1959.....	3½	100.0	100.1	3.14
96 September 15, 1959.....	3½	99.31	100.1	3.13
80 January 15, 1960.....	3.80	99.22	99.25	4.22
199 February 15, 1960.....	4½	99.23	99.26	4.68
w.i. February 15, 1960.....	4½	99.31	100.1	4.81
124 March 15, 1960.....	4½	99.26	99.29	4.63
275 April 15, 1963.....	3½	95.12	95.28	4.33

Banks for cooperatives

Outstanding—millions	Rate	Bid	Ask	Yield
78 August 1959.....	3.55	100.0	100.1	2.64
77 October 1959.....	3½	99.29	99.31	3.62
130 December 1959.....	4½	100.1	100.3	3.96
w.i. February 1960.....	4½	99.30	100.0	4.87

Treasury bills

Outstanding		Bid (percent)	Asked (percent)	Outstanding		Bid (percent)	Asked (percent)
Millions	Maturity			Millions	Maturity		
1,400	July 23.....	2.55	2.30	400	Nov. 5.....	3.28	3.18
1,402	July 30.....	2.55	2.30	400	Nov. 12.....	3.28	3.18
1,400	Aug. 6.....	2.55	2.30	400	Nov. 19.....	3.30	3.20
1,400	Aug. 13.....	2.55	2.30	400	Nov. 27.....	3.34	3.24
1,401	Aug. 20.....	2.60	2.45	400	Dec. 3.....	3.34	3.24
1,395	Aug. 27.....	2.65	2.50	500	Dec. 10.....	3.36	3.26
1,500	Sept. 3.....	2.65	2.50	500	Dec. 17.....	3.38	3.28
1,600	Sept. 10.....	2.70	2.60	1,500	Dec. 22.....	3.38	3.28
1,600	Sept. 17.....	2.80	2.70	500	Dec. 24.....	3.42	3.32
1,501	Sept. 21.....	2.92	2.82	500	Dec. 31.....	3.80	3.74
1,600	Sept. 24.....	3.04	2.94	400	Jan. 7, 1960.....	3.83	3.78
1,600	Oct. 1.....	3.10	3.00	400	Jan. 14.....	3.85	3.80
1,600	Oct. 8.....	3.20	3.20	2,006	Jan. 15.....	3.86	3.80
1,600	Oct. 15.....	3.28	3.22	3,000	Mar. 22.....	4.22	4.19
400	Oct. 22.....	3.30	3.20	2,003	Apr. 1.....	4.22	4.19
400	Oct. 29.....	3.30	3.20	2,000	July 15.....	4.48	4.45

Federal Land Bank bonds

Outstanding millions	Rate	Bid	Ask	Yield
164 October 1959.....	13 $\frac{1}{4}$	99.14	99.16	3.77
89 February 1960.....	3 $\frac{3}{4}$	99.16	99.20	4.49
124 February 1960.....	2 $\frac{1}{4}$	98.30	99.2	4.08
201 April 1960.....	3 $\frac{3}{8}$	99.12	99.16	4.56
107 June 1960.....	2 $\frac{1}{2}$	98.14	98.18	4.22
83 April 1961.....	3 $\frac{3}{8}$	98.4	98.12	4.38
130 September 1961.....	4	99.6	99.14	4.27
125 May 1962.....	4	99.6	99.14	4.21
122 May 1963.....	2 $\frac{3}{4}$	93.8	93.24	4.57
108 May 1966.....	3 $\frac{3}{4}$	91.28	92.12	4.57
72 February 1872-67.....	4 $\frac{3}{8}$	95.0	96.0	4.55
75 October 1870-67.....	4 $\frac{1}{2}$	99.8	100.8	4.46
86 March 1968.....	4 $\frac{1}{4}$	98.4	98.20	4.44
100 March 1969.....	4 $\frac{3}{8}$	98.0	99.0	4.50
60 July 1969.....	4 $\frac{3}{8}$	100.0	101.0	4.50
83 April 1970.....	3 $\frac{1}{2}$	91.0	92.0	4.45
60 May 1971.....	3 $\frac{1}{2}$	90.0	91.0	4.49
109 September 1972.....	3 $\frac{1}{2}$	93.0	94.0	4.48

Federal National Mortgage Association

Outstanding millions	Rate	Bid	Ask	Yield
100 August 1959.....	3 $\frac{7}{8}$	100.0	100.2	2.61
100 October 1959.....	3 $\frac{3}{4}$	99.31	100.1	3.55
100 December 1959.....	3 $\frac{3}{4}$	99.26	99.30	3.88
150 March 1960.....	4 $\frac{1}{2}$	99.26	99.29	4.63
100 June 1960.....	4	99.10	99.16	4.58
797 August 1960.....	3 $\frac{3}{8}$	98.20	98.26	4.74
200 February 1962.....	3 $\frac{1}{2}$	97.0	97.8	4.65
150 March 1963.....	3 $\frac{3}{4}$	95.0	95.8	4.68
100 November 1963.....	4 $\frac{3}{8}$	98.4	98.12	4.55
100 June 1965.....	4 $\frac{3}{8}$	98.16	98.28	4.59
100 March 1968.....	3 $\frac{1}{2}$	92.16	93.0	4.61
90 April 1969.....	4 $\frac{3}{8}$	98.0	98.8	4.60

International Bank bonds

Outstanding millions	Rate	Bid	Ask	Yield
150 May 1968.....	3 $\frac{3}{4}$	92.0	93.0	4.71
100 January 1969.....	3 $\frac{1}{2}$	91.0	92.16	4.49
60 October 1971.....	3 $\frac{1}{2}$	90.0	92.0	4.35
150 July 1972.....	3	83.16	85.0	4.55
100 December 1973.....	4 $\frac{1}{2}$	98.16	99.16	4.55
50 May 1975.....	3 $\frac{3}{8}$	87.0	89.0	4.34
50 March 1976.....	3	81.0	83.0	4.45
100 January 1977.....	4 $\frac{1}{2}$	98.0	99.0	4.58
100 May 1978.....	4 $\frac{1}{4}$	94.0	95.0	4.65
50 January 1979.....	4 $\frac{1}{4}$	94.0	95.0	4.65
75 November 1980.....	4 $\frac{1}{4}$	98.16	99.16	4.78
100 October 1981.....	3 $\frac{3}{4}$	81.16	83.0	4.46

The following quotation for the IB serial issues represents the highest and lowest yields for all maturities:

Outstanding millions	Rate	Bid	Ask	Yield
40 1959-62.....	2	4.25	3.25	-----

Federal Government issues of certificates, notes, and bonds: By purpose of issue, 1945-58

[Dollar amounts in billions ¹]

Year	Total (1)	New money (2)	Refunding (3)	Col. (2), col. (1) (4)	Col. (3), col. (1) (5)
1945	\$74.1	\$39.6	\$34.5	<i>Percent</i> 53.4	<i>Percent</i> 46.6
1946	30.0		30.0		100.0
1947	28.8		28.8		100.0
1948	30.1		30.1		100.0
1949	34.0		34.0		100.0
1950	38.1		38.1		100.0
1951	30.6		30.6		100.0
1952	33.7	4.2	29.5	12.5	87.5
1953	44.2	9.3	34.9	21.0	79.0
1954	59.7	10.1	49.6	16.9	83.1
1955	49.2	11.7	37.5	23.8	76.2
1956	33.6	3.2	30.4	9.5	90.5
1957	55.8	9.1	46.7	16.3	83.7
1958	62.2	11.3	50.9	18.2	81.8

¹ Source: Treasury Bulletins.

State and local governments, securities issues: By purpose of issue, 1945-58

[Dollar amounts in billions ¹]

Year	Total (1)	New capital (2)	Refunding (3)	Col. (2), col. (1) (4)	Col. (3), col. (1) (5)
1945	\$0.8	\$0.5	\$0.3	<i>Percent</i> 62.5	<i>Percent</i> 37.5
1946	1.2	1.0	.2	83.4	16.7
1947	2.4	2.3	.1	95.8	4.2
1948	3.0	2.8	.2	93.3	6.7
1949	3.0	2.9	.1	96.6	3.4
1950	3.7	3.6	.1	97.3	2.7
1951	3.3	3.2	.1	97.0	3.0
1952	4.4	4.1	.3	93.2	6.8
1953	5.6	5.5	.1	98.2	1.8
1954	7.0	6.8	.2	97.1	2.9
1955	6.0	5.9	.1	98.3	1.7
1956	5.4	5.3	.1	98.1	1.9
1957	7.2	7.1	.1	98.6	1.4
1958	7.8	7.7	.1	98.7	1.3

¹ Sources: 1957-58, Investment Bankers Association; 1946-56, Bond Buyer. The 2 series are not directly comparable.

Total securities issues of the Federal Government, State and local governments, and corporations: By purpose of issue, 1945-58

[Dollar amounts in billions]

Year	Total issues ¹	Total securities issues for new capital ²	Total securities issues for refunding	Col. (2) ÷ col. (1)	Col. (3) ÷ col. (1)
	(1)	(2)	(3)	(4)	(5)
1945.....	\$80.8	\$41.4	\$39.4	(Percent) 51.2	(Percent) 48.8
1946.....	38.0	4.9	33.1	12.9	87.1
1947.....	37.7	7.4	30.3	19.6	80.4
1948.....	40.1	9.5	30.6	23.7	76.3
1949.....	43.0	8.5	34.5	19.8	80.2
1950.....	48.1	8.6	39.5	17.9	82.1
1951.....	41.5	10.3	31.2	24.8	75.2
1952.....	47.5	17.0	30.5	35.8	64.2
1953.....	58.6	23.3	35.3	39.8	60.2
1954.....	76.1	24.4	51.7	32.1	67.9
1955.....	65.2	26.4	38.8	40.5	59.5
1956.....	49.7	18.9	30.9	38.0	62.0
1957.....	75.7	28.6	47.0	37.8	62.2
1958.....	81.4	29.8	51.6	36.6	63.4

¹ Securities issues of the Federal Government includes only certificates, notes, and bonds.

² The Federal Government component is new money.

*Source: Securities and Exchange Commission.

*Corporations' securities issues: By purpose of issue, 1945-58**

[Dollar amounts in billions]

Year	Total issues ¹	Total securities issues for new capital ²	Total securities issues for refunding	Col. (2) ÷ col. (1)	Col. (3) ÷ col. (1)
	(1)	(2) ³	(3) ³	(4)	(5)
1945.....	\$5.9	\$1.3	\$4.6	(Percent) 22.0	(Percent) 78.0
1946.....	6.8	3.9	2.9	57.4	42.6
1947.....	6.5	5.1	1.4	78.5	21.5
1948.....	7.0	6.7	.3	95.7	4.3
1949.....	6.0	5.6	.4	93.3	6.7
1950.....	6.3	5.0	1.3	79.4	20.6
1951.....	7.6	7.1	.5	93.4	6.6
1952.....	9.4	8.7	.7	92.6	7.4
1953.....	8.8	8.5	.3	96.6	3.4
1954.....	9.4	7.5	1.9	79.8	20.2
1955.....	10.0	8.8	1.2	88.0	12.0
1956.....	10.7	10.4	.4	96.3	3.7
1957.....	12.7	12.4	.2	98.3	1.6
1958.....	11.4	10.8	.6	94.7	5.3

¹ Securities issues of the Federal Government includes only certificates, notes, and bonds.

² The Federal Government component is new money.

³ Cols. (2) and (3) may not add to total because of rounding.

*Source: Securities and Exchange Commission.

*Average maturity of the Federal marketable interest-bearing public debt:
Semiannually, December 1949 through December 1958¹*

End of period	Average maturity		End of period	Average maturity	
	Years	Months		Years	Months
1949—December.....	8	9.0	1954—December.....	5	5.9
1950—June.....	8	2.5	1955—June.....	6	9.6
December.....	8	1.1	December.....	6	5.5
1951—June ²	6	6.8	1956—June.....	5	4.5
December.....	6	1.0	December.....	4	10.8
1952—June.....	5	8.4	1957—June.....	4	9.3
December.....	5	3.3	December.....	4	6.6
1953—June.....	5	3.8	1958—June.....	5	2.9
December.....	5	2	December.....	4	9.3
1954—June.....	5	6.0			

¹ Source: Treasury Department. All issues classified by final maturity date, except partially tax-exempt bonds which are classified by earliest call date.

² On Apr. 1, 1951, the Treasury offered holders of a 2½-percent bond an exchange for 2¾-percent investment bonds, series B, maturing Apr. 1, 1980. The new securities were exchangeable for 1½-percent marketable notes, but were nonmarketable as such. Thus, the rather sharp drop in the average maturity of the debt over the first 6 months of 1951.

Total debt and Federal debt: Selected years, 1929-58

[In billions of dollars]

End of year	Total gross debt	Total gross Federal debt	Total gross Federal debt as percent of total gross debt
1929.....	\$214.4	\$16.3	7.60
1934.....	197.3	28.5	14.45
1939.....	207.7	41.9	20.17
1944.....	430.9	232.14	53.87
1945.....	463.3	278.7	60.15
1946.....	457.9	259.4	56.65
1947.....	485.6	257.0	52.92
1948.....	498.6	252.9	50.72
1949.....	520.3	257.2	49.43
1950.....	566.4	256.7	45.32
1951.....	607.5	259.5	42.72
1952.....	646.0	267.4	41.39
1953.....	683.6	275.2	40.26
1954.....	714.0	278.8	39.05
1955.....	786.2	280.8	35.72
1956.....	830.7	276.7	33.31
1957.....	865.1	275.0	31.79
1958.....	901.8	283.0	31.38

Sources: "Total Gross Debt," Survey of Current Business, September 1953, May 1957, May 1959. "Total Gross Federal Debt," Federal Reserve Bulletins.

Representative CURTIS. Getting to the questions Mr. Reuss has raised, I want to clarify a few questions.

First of all, the letter Mr. Reuss has referred to was in response to a request from the Republican members of the Ways and Means Committee to state your position. Is that not true?

Mr. MARTIN. That is correct.

Representative CURTIS. I wanted it clear that it was at our request that this was done.

Secondly, that Mr. Reuss in his interrogation seems to separate the speeches and the context of his amendment from the amendment itself. He says that they had nothing to do with each other.

I think there is the basic disagreement, at least as far as I am concerned. I do not quite see how you can separate the context of the

amendment that deals with this very subject of the question of maintaining an adequate or an inadequate or a too great money supply, from this issue. Mr. Reuss, Mr. Patman, Mr. Johnson, Senator Douglas, and the Democratic National Policy Committee, have all commented on this thing.

Furthermore, the so-called Reuss amendment, such as it is presently, is by no means the original Reuss proposal. It has been considerably watered down and, as I said somewhat facetiously but not entirely so when Secretary Anderson was testifying, if it were watered down to where it said nothing, then we could go along; but if it actually did say something, then we felt that it would be dangerous.

Representative REUSS. Mr. Chairman, will the gentleman yield?

Representative CURTIS. Certainly I will yield.

Representative REUSS. I just want to correct the record as to "the so-called Reuss amendment."

I am quite ready to not have my name attached to it, rather than have it called the so-called Reuss amendment.

The sense-of-Congress amendment was first submitted by me as House Concurrent Resolution 196 almost 2 months ago. It was referred to the Banking and Currency Committee. This was before the administration had asked for its interest rate increase. It was then, in exactly those words, un-watered-down, offered by me in my testimony before the House Ways and Means Committee, and it was adopted, again in those words, without any watering down or weakening, by the Ways and Means Committee.

Representative CURTIS. Oh, no.

Representative REUSS. So I want it clear that I knew what I was proposing in the beginning, I did in the middle, and I will stand by it now, I hope, to the end.

Representative CURTIS. I happen to have kept the various mimeographed copies as we corrected and worked over this language, and the reason I called it the so-called Reuss amendment is that there is no question as to the original language that the gentleman from Wisconsin used that language as then proposed by Congressman Metcalf, I believe, in the Ways and Means Committee. There has been considerable alteration of the language, and I do not believe that what the Ways and Means Committee tentatively approved—and I might say some of those who were opposed to anything going out, voted for it simply to get the bill out.

That is why I made the point to the gentleman the other day, that I doubted very much whether the majority of the Ways and Means Committee were in favor of any amendment along these lines.

Representative REUSS. Of course, I assume that people when they vote for something are for it. Perhaps that was incorrect.

Representative CURTIS. The gentleman is a sufficient politician and sufficiently aware of the procedures of Congress to know that that frequently is the case. We have another situation with the labor bill, where it is doubtful whether the bill that the committee passed out has majority approval, but many people feel that the House ought to work its will on this legislation.

Certainly that is the position in regard to this interest ceiling bill. I voted it out because, even though I disagreed with the Reuss amendment, I felt that we had studied it sufficiently so that the House could

debate it intelligently. And it is not the first time I have voted out a bill with which I disagreed.

But, to get back to the merits of this thing, what has been approved in the Ways and Means Committee is not the original language that the gentleman proposed. It has been watered down considerably and has been altered and is still, according to Speaker Rayburn's press release, subject to discussion as to whether it can be worded in different ways.

But essentially I think it must be taken in context with the gentleman from Wisconsin's speeches on the floor and the criticism that has been directed just recently. Incidentally, in Speaker Rayburn's press release, the criticism of the Federal Reserve—and this is a question I might direct to the witness:

Is it not true that the reaction to this abroad and in this country is that there is criticism of what the Federal Reserve Board has been doing in this area? Has it not been interpreted as adverse criticism?

Mr. MARTIN. That is pretty difficult, Mr. Curtis, to say how widely people have thought about it. My feeling is, as I stated in the letter which we are now getting for Mr. Reuss, that thoughtful people will interpret it as a lack of determination on the part of this country to meet the current situation in a sound way.

Representative CURTIS. The thing I am getting at, Mr. Martin, is that this amendment, however it is worded, comes from a background and context of direct and open criticism of the Federal Reserve, and I think that it is very proper that people who think it should be criticized do so. That is not what I am objecting to or pointing out. It comes from that context, so, however it is worded, in my judgment it is apt to be interpreted as being direct criticism as to what they have been doing.

As I understand what the gentleman has testified to openly, and certainly before the Ways and Means Committee, in essence, the Federal Reserve has been trying, within the limits of what I understand you to believe is its basic duty, to preserve the value of money, to be of assistance to the Treasury. Is that correct?

Mr. MARTIN. That is absolutely correct. We have done everything in our power, and as I testified before the Ways and Means Committee, and I am glad to reiterate here, if there has been a bias in our activities, it has been a bias in favor of leaning over backward to help the Treasury, even though at times we have wondered whether we were going too far. We have never compromised with the principle, but the bias has been toward easy money, in order not to embarrass the Treasury in anything that they have been doing. That has been our conscious, deliberate position. Time after time in open market meetings it has come up, and the question has been whether we would do this, that, or the other thing, and we always ask the question, "Will it harm or help the Treasury at this particular juncture?" I think that is perfectly appropriate.

Representative CURTIS. Thank you, Mr. Martin.

One other aspect of the context from which this amendment comes, and which I regret, I might say, and one on which I have tried to take issue with the gentleman, is that it comes from an attack on this administration, on the alleged grounds that this administration and the Federal Reserve are responsible for high interest rates; and the

other side of the coin, that the Democratic leaders, including Mr. Reuss, are against high interest rates, and therefore those who are against them are in favor of high interest rates.

I view the Reuss amendment as no more than an attempt to get off the hook of that untenable economic position of trying to maintain that they are for lower interest rates and the present administration is for higher interest rates, and that by voting for a bill that removes an interest ceiling, they will have watered down that argument as they might present it to the people.

It is in that context, too, that the Reuss amendment must be viewed. I think when the gentleman tries to now separate it from the political overtones he and his allies have created, having been borne in political attack, he has an extremely difficult task. I think the gentleman in fairness should say yes, that it is borne with political overtones, and that the gentleman believes in that point of view. But let us not now try to present it as if it were an economic problem entirely.

Representative REUSS. Will the gentleman yield?

Representative CURTIS. I will certainly do so.

Representative REUSS. My position is very clear. I have felt for some time that the Federal Reserve was not adding to the money supply sufficiently for the needs of a growing economy. This is an entirely separate controversy. I will continue my attacks on the Federal Reserve until either I am not here any more, or the Federal Reserve changes its policy. That, however, is quite a different matter, and not related to that which we are discussing here.

The amendment we are discussing here is completely neutral on the question of how much money is created or whether any money is created. It simply says that where it is created, do so not like you have been doing in the last 5 or 6 years but in a manner calculated to help the taxpayers and the Treasury, a subject which we will return to later. I do not want to encroach on your time now further than to say this, Mr. Curtis—

Representative CURTIS. I just want to comment on that one thing.

That, I think, is fair argument. I disagree with it, but I think that is fine. If it is confined to that, that will be good.

Now your second point?

Representative REUSS. I will just make the point that because a given Congressman or a set of Congressmen or a number of members of one political party hold views on subject A, it does not therefore follow that subject B can avoid being subjected to debate on its merits. And what subject B, that is, the so-called sense resolution, says is: Irrespective of the policy as to the rate of monetary expansion or as to whether there should be any monetary expansion at all, does it not make better sense in a time of crisis in the national debt for the Federal Reserve to do what it can, consistent with its view of a sound monetary policy, to help the Treasury?

That is the issue, and bringing in outside considerations about what I or Senator Johnson or Mr. Rayburn or Mr. Patman or Mr. Coffin or Senator Douglas or anybody else thinks about the Federal Reserve's general policy of the rate of monetary expansion does not seem to me to meet the issue.

I would hope that the gentleman would address himself to the specific amendment that we have proposed, and, if he has objections

to it, state exactly what they are so the press and the public can know what it is all about.

Representative CURTIS. We have done that, too; but the point the gentleman raises is that he thinks he can separate the two.

I do not believe it ever was intended that they be separate; that they were presented in that context. Now that we have raised this issue, the gentleman seeks to separate it from his previous criticism. But the fact remains that instead of going before the Banking and Currency Committee, which has jurisdiction over this matter—and the gentleman is a member of that committee—this was brought before the Ways and Means Committee, which really has no background and experience in the details of the Federal Reserve Act, asking us in an interest ceiling bill, having to do with debt management, for us in effect to say something to the Federal Reserve which comes from those who are great and open critics of the Federal Reserve. How else would it be interpreted than as adverse criticism?

That is the point, and the Secretary of the Treasury and Mr. Martin, I believe, have both pointed out that psychology plays a very great part in this area. I think the gentleman would agree with that, would he not?

Representative REUSS. I would agree, but I think it is up to the leadership in this country to provide a wholesome and proper public psychology, both here and abroad. I think seeing ghosts under beds and misinterpreting the actions of the Ways and Means Committee is not a very good way to do that.

Representative CURTIS. If the gentleman would only join in trying to present to the public a real clear picture of it, No. 1, by emphasizing to the public that the Federal Reserve is not a creature of the executive department, but is, in essence, an independent body, but if anything, it is a creature of the Congress. Yet the speeches of the gentleman and his associates have created the impression, whether intentionally or not, that the interest policy pursued by the Federal Reserve is the administration's doing.

Representative REUSS. Oh, no; not because of anything the Federal Reserve has done, but because the administration has openly and repeatedly embraced the policies of the Federal Reserve and said they are fine.

Representative CURTIS. That is fair because it is true, but it is two separate groups arriving at the same conclusion.

Representative REUSS. Well, I have been fair.

Representative CURTIS. The question is, what amounts of fairness, not that the gentleman's intentions are not to be fair, but as to whether or not what he has actually done amounts to fairness.

Representative PATMAN. Mr. Coffin.

Representative COFFIN. Thank you, Mr. Chairman.

Mr. Martin, I think it is perhaps generally understood what a disorderly house is. What is your definition of a "disorderly market"?

Mr. MARTIN. It is a very difficult definition to give, Mr. Coffin, but I think that a "disorderly market" is one in which large sell orders are pouring into the market from sellers who do not need to sell and there are no successive bids, so that panic takes over the market, and there are no sales possible at any price; in other words, continuous buying and selling comes to a halt and the market as a place of continuous transactions just stops.

Representative COFFIN. That, then, would be the height of disorder, would it not?

Mr. MARTIN. Yes.

Representative COFFIN. It would be a chaotic market.

Mr. MARTIN. It would be disorderly—even chaotic.

We had in our directive, during the time of a pegged market, maintaining orderly conditions in the Government securities market. When we moved away from the peg, we tried to not absolve ourselves or abdicate our responsibility to see that the market did not fall apart, but to see that the market was given an opportunity to make adjustments that were reasonable within a reasonable framework. Therefore, after long discussion of it, we finally came to this phrase "a disorderly market." I am not on the desk which is watching it all the time, and it might be good for Mr. Roosa to comment on that. He was up there.

Would you like to comment?

Would you object to his commenting on the disorderly market?

Representative COFFIN. No; I certainly would not, but, before that, does the Federal Reserve have any memorandum that helps it decide when a market is disorderly? Do you have criteria, do you have anything in writing that helps you come to a decision as to the circumstances that would make you say that a market is disorderly?

Mr. MARTIN. Yes; I think we have. I will ask Mr. Roosa to comment on that because he has been right in the market on a number of occasions.

Representative PATMAN. He is manager of the account, is he not?

Mr. MARTIN. No.

Mr. ROOSA. No; I have a name similar to that of the manager, and for nearly 3 years I worked as his deputy. I am no longer assigned to work connected with the actual management of the account, but I am in the New Work Reserve Bank, and of course, being in the research department, I do have continuous contact with the management of the account because one of our tasks is to try to analyze current experience for the purpose of learning for the future.

One of the efforts we undertake in cooperation with the permanent staff of the account itself is to study every situation that has verged on or been disorderly, with a view to trying to sort out those elements in the situation that lead us toward a clearer comprehensive view for the future.

The essence of these markets is that they are always changing, that no single set of benchmarks will ever serve. The first signs of impending disorder are usually those of a congestion of sell orders for which there are no matching bidding interests, and what we call a price vacuum begins to develop. The incipient signs of this pattern of development can occur in a wide variety of ways, and we have to be alert to send word to the members of the Open Market Committee, which we do through immediate telephone communication to the Chairman and then through reporting the details as we see them in the given circumstances, and alerting the members of the Federal Open Market Committee that disorder may develop.

I did not happen to be present last summer, I was away at the time, but this certainly was the pattern that was followed then.

Representative COFFIN. Let me ask about last spring. As the difference in yields between short terms and long terms became substan-

tial, did anything happen in the Federal Reserve? Were any danger signals hoisted to the yardarm?

Mr. ROOSA. It would not only be the length or width of the spread between short and long rates, but certainly a feeling of some alert unease in our own appraisal of the market situation began even in May, and we were particularly concerned as we watched the reactions to the subscriptions on the exchange offering at that time, and were, of course, further concerned as we saw the signs of speculative buildup, and were, within the limits that are proper and under the authority of the Open Market Committee, interested in going into the details of credit situations where that was appropriate, to try to ascertain what was going on.

But these are matters that I think you gentlemen will have an opportunity to discuss with the men who really know, such as Mr. Rouse himself. I believe you are scheduled to meet with him in New York soon. I suggest that he could give you a chapter and verse account. You may also find that the tentative draft of part II of the Treasury-Federal Reserve Study provides an adequate account of the various developments.

Representative COFFIN. To sum up your own testimony, do I understand that there is anything in writing setting forth various situations which could be considered components of disorder?

Mr. ROOSA. Yes, indeed. There is a series of memorandums in the nature of working memorandums. These things are not ever sorted out in one single page that could readily be handed over to someone who does not work with these things day in and day out, and is fully familiar with a lot of the jargon, but certainly from among the memorandums prepared, and these are being prepared continually, extracted manuscripts could be made available.

Representative COFFIN. Would it be feasible to cull out, in language that I could understand, a fair summary of the components of disorder as you from time to time have isolated them and articulated them?

Mr. ROOSA. Yes, sir, that could be done.

Representative COFFIN. I would be very interested.

Mr. MARTIN. We would be glad to get that for you, Mr. Coffin. I might say that there is hardly a day goes by that that is not considered. (The item referred to follows:)

WHAT CONSTITUTES DISORDERLY CONDITIONS IN THE GOVERNMENT SECURITIES MARKET

The general conception of disorderly market conditions in the Government securities market envisions a situation in which selling "feeds on itself," that is, a situation in which a fall in prices, instead of eliciting an increase in the amount of securities demanded and a decrease in the amount supplied, elicits the reverse—a falling away of bids and a rise in both the number and the size of offerings. Temporarily, there is no price level which will clear the market. The presence of these technical conditions, however, may not always be enough to warrant finding of "disorderly conditions," for other factors which accompany them or cause them must be considered, and these other factors must be appraised in terms of the extent to which they affect or contribute to market psychology. In this regard, the Open Market Committee in arriving at its finding of "disorderly conditions" in July 1958 was influenced, not only by the rapid falling away of prices and the virtual absence of bids in the face of a multiplication of offerings, but also by the threat of almost certain failure in a major

Treasury refunding operation and by the development of a highly precarious international, political, and military situation. These factors contributed importantly to a demoralized atmosphere in which potential buyers appeared unwilling for a time to commit at almost any price.

It is thus evident that the problem of determining what constitutes disorderly conditions is a very difficult one. It is clear that price movement alone would not ordinarily justify a finding that a disorderly market exists (although such a movement would nevertheless require careful consideration of its causes and possible consequences). Even rapid price change, accompanied by minimal trading, might not constitute a disorderly market condition if increased offerings were not being pressed on the market and, most important, if the price adjustment were occurring in an atmosphere free of panic.

In general, three conditions would ordinarily have to exist to justify a finding of disorder: Spiralling price changes that tend to "feed upon themselves"; a trading vacuum accompanied by a buildup in the number and size of offerings and by a disappearance of bids; and a disorganized market psychology. The emergence of such conditions might be caused by or be coincident with major international or domestic political developments or a Treasury financing operation, although market disorder could conceivably develop in the absence of such external influence. This definition is, necessarily, general rather than precise; a determination that disorder exists in a particular market situation must rest upon appraisal of the combination of circumstances at the time, rather than upon application of firm criteria.

Representative COFFIN. I could imagine this might involve many, many memorandums. I would not expect you to go through everything that you have ever done that could remotely be related to this, but a fair summary of the work you have done.

Now, Mr. Martin, you were, I take it, alertly uneasy last spring, but it was not until after the Treasury had moved into the situation in late June and early July that the Federal Reserve finally, in latter July, moved into the market. If you had this to do over again, would you concede that the Federal Reserve's earlier entrance into the market would have been a helpful thing?

Mr. MARTIN. No, quite the reverse, Mr. Coffin. I do not think we had any clear indication of anything that could be done. We must remember that it was Iraq and the landing in Lebanon that really precipitated our going in, and also a Treasury financing that came at that particular juncture. Although we looked at it constantly day in and day out, and I spent a good many evenings reviewing the reports from the New York people and the data that we have in the Board, and I know that other members of the Board did also, it was not until we got a combination of the Iraq-Lebanon situation and the Treasury financing that we felt we had a situation that was completely disorderly and that warranted our intervening.

Representative COFFIN. Is this a fair summary from what you two gentlemen have said: That your criteria of disorder are a very high threshold. It has to be, as you say, completely disorderly, with something of the magnitude of an Iraq and Lebanon incident, to make you take advantage of your exception in the 1951 accord?

Mr. MARTIN. I do not think it has to be an Iraq or a Lebanon, but it has to be a situation that we feel is unmanageable by the market itself.

You must remember, Mr. Coffin, that in the period when we were moving into a freer market, frequently when the Treasury would announce a financing it would be reported as favorably received, and then on the following Monday night, let us say, when the books were opened, there would be a whole lot of rumors that it was going to

fail completely, and unless the Federal Reserve came in it would just collapse.

We resisted that in several instances, and it went over with a bang, because we had for quite a time during a period of the evolution moving out of a pegged market, gotten to be at the mercy of these rumors, sometimes originating with dealers. Frequently market participants were merely trying to see how far they could push us before we would actively come in; and every time we came in we would acquire a great many more securities than were wanted for monetary policy. It became highly questionable whether it was a legitimate monetary operation.

Representative COFFIN. It seems to me we are in a dilemma, because you start off your statement saying how lucky we are to have a market with these skilled, sensitive dealers, who take so much initiative and incur so much risk, and you are quite happy with the market as it substantially exists. Now we find that they are still rumor mongers on occasion.

Mr. MARTIN. All markets are that way.

Representative COFFIN. Mr. Chairman, will you tell me when my time is up? I am afraid I transgressed.

Representative PATMAN. You have 3 more minutes.

Representative COFFIN. Will you tell me what the rationale of your bills-only policy is?

Mr. MARTIN. To try to get as strong and resilient a market as we can possibly have, just to avoid the sort of thing I was just talking about.

Representative COFFIN. That explains why you do not want to go beyond bills. But why do you go into bills?

Mr. MARTIN. Because in order to make adjustments in the money market, we have from time to time to do it through the medium of securities.

Representative COFFIN. But this is an infringement on competition as a mechanism to adjust the money market?

Mr. MARTIN. Yes, there is no question about it. But we seek to reduce that infringement to the minimum.

Representative COFFIN. So a little sin is all right?

Mr. MARTIN. It is not a case of a little sin. I think we crossed that bridge when we came to the Federal Reserve Act and decided we would have a managed currency and decided to give this authority, this trusteeship over the money into the hands of a group of people—I do not like the use of the word “experts”—who are supposed to be devoting their full time to it, and that they would make proper adjustments when necessary or appropriate.

Representative COFFIN. We are talking now about 10 nonbank dealers and 7 bank dealers.

Mr. MARTIN. I was referring to people in the Federal Reserve. As to dealers, there are about 12 nonbank dealers and about 5 bank dealers.

Representative COFFIN. Yes, my figures were wrong.

Mr. MARTIN. And we could, perhaps, have more dealers. We made an exhaustive study of this in 1952 in what we called an ad hoc committee report. Recently, we have been doing it again, because this has to be continuous study. I think a lot of improvements can be

made. I do not want to give the impression that I think this market is perfect.

Representative COFFIN. I believe you overstate your position on page 6 of your statement, where in your argument against going beyond the bills only, you just paint a picture of pushing it to the extent where all private investors go into short terms and the Government is saddled with nothing but long-term securities, which seems to be pretty remote from our present-day picture; and the Government system would put itself, you say, into a frozen portfolio position.

This seems to be really setting up a straw man that just does not exist.

Mr. MARTIN. That may be. I was just trying to put in the ultimates of where you could go on it.

Representative COFFIN. You yourself earlier said that the debate is not in terms of ultimates; it is in terms of degree.

Mr. MARTIN. That is right. I was trying to establish what the process could be.

Representative COFFIN. It could be, unless the Federal Reserve has plenty of other tools to work with to prevent this from happening, even if it did not restrict itself to bills only.

Mr. MARTIN. Let me try to put this in the way I see it, as one who has been a broker a good part of his life, and that is about all.

The real problem here has been that for a long time the Treasury has been at the mercy of the market. Being the largest demander on the market, it has had to come, hat in hand. The real problem on financing with short-term versus long-term securities at the present time can be put very simply. The U.S. Government is in about the same position that you would be as an individual if you had time payments coming due on an automobile, a refrigerator, and a television set, and you had a mortgage on your house that instead of being financed for 20 or 25 years was coming due every 90 days, and you had not been able to accumulate any savings so that you did not have much in the way of reserves. Then you would be going to the market and saying, "Well, now, these notes, and charge accounts are due, and I don't have the money to pay them, so I have to borrow some more money."

Under those circumstances you would be pretty much dependent upon paying what the market asked.

For quite a time, there has been denied to the Treasury the tools to deal with its problem. Consequently, the Treasury has had constantly to move into shorter term securities. Part of the problem, as I have said here, is due to the fact that the Federal Reserve has been trying as hard as it can to help the Treasury, though I am not sure we have really helped them every time.

Representative COFFIN. I know my time is up, Mr. Chairman, but I just want to throw out my reaction to your statement about being hat in hand.

I think it is true, but I would have thought that to have available from time to time this tool of going in on the market for long terms is one that would make you not quite so helpless.

Mr. MARTIN. And it should not be disregarded. I think you have made a very fair comment.

I do not want to overstate the problem as such, but I want to say, as one who has had some experience in markets, that it is awfully easy to take some steps down a path and then find that you cannot retrace your steps. We have been trying as hard as we can, without being dogmatic or stubborn about it, to avoid moving down a road from which we will not be able to retrace our steps. It is a very difficult thing to do.

Representative COFFIN. Thank you.

Representative PATMAN. Mr. Widnall.

Representative WIDNALL. Mr. Martin, in your statement you said that speculation financed by credit created a particular problem in 1958 because there were large blocks of holdings acquired by newcomers to the market who bought or made commitments to buy Government securities on very thin margin or in many cases on no margin at all.

Let me understand better the operation of that market. How does it differ from the regular stock market by way of margin requirements? Is there no control over margin in the bond market?

Mr. MARTIN. No; there is no prescription.

Mr. YOUNG. That is right. Government securities are exempt from margin regulation under the provisions of the Securities and Exchange Act of 1934, which provides authority for margin regulation on securities listed on stock exchanges.

Mr. MARTIN. There is a general rule; most brokers, I think, require 5 percent. They did when I was in the business. This has been a long time ago. What they do now I am not sure.

Representative WIDNALL. What is the purpose of that exemption?

Mr. MARTIN. It was thought that it might help the Government securities market. We were trying to do everything we could to be helpful to the Government securities market, and I think Secretary Morgenthau thought that that was a very important point. He was Secretary of the Treasury at that time.

Representative WIDNALL. In view of this recent experience, do you think it would be helpful or harmful to require margin requirements in bond purchasing?

Mr. MARTIN. I am inclined to think there ought to be some margin on them at all times.

The thing that worried me most in this was not the specific purchases as much as the use of repurchase agreements, a type of credit on which there was no margin at all. To me that kind of lending is wrong.

Representative WIDNALL. So it lends itself to pure speculation.

Mr. MARTIN. It lends itself to pure speculation and to abuse.

There was speculation on the 2 $\frac{3}{8}$ bonds issued in June of last year, speculation of all types, a great deal of it on a cash basis, which was unfortunate, too, and quite a lot on a credit basis. You had a situation where it would have been desirable, in my judgment, to have had some credit limitation, even if it was not fully effective.

You know the stock exchange disciplined one firm for its activities in this speculative field.

Representative WIDNALL. As I understand also from your statement.

The outright holdings at that time largely represented subscriptions on the part of commercial banks and business corporations, and

the speculative portion of the market was held by others. In other words, they were not in and out of it as much as the others.

Mr. MARTIN. That is right.

Representative WIDNALL. What percentage of the Government debt is held today by the series E bondholders? A very small portion of it?

Mr. MARTIN. Series E, no; it is not a sizable proportion. About 10 percent, Mr. Roosa says.

Representative PATMAN. I figured about 15 percent; of course, I am not taking issue with you, Mr. Martin.

Mr. MARTIN. It is all right, Mr. Patman.

Representative WIDNALL. I would like to have the exact figures if they are available.

Mr. MARTIN. We will get those for you, Mr. Widnall.

(The figures requested by Mr. Widnall are in the table which follows. Those relating to the volume of savings bonds outstanding include, of course, accrued interest.)

Ratio of outstanding series E and H savings bonds to gross public debt, 1954-59

As of June—	Total gross public debt ¹	E bonds outstanding	Percent of total	E & H bonds outstanding	Percent of total
1954.....	271.260	36.458	13.4	37.482	13.8
1955.....	274.374	37.186	13.6	39.285	14.3
1956.....	272.751	37.898	13.9	40.929	15.0
1957.....	270.527	37.969	14.0	41.498	15.3
1958.....	276.343	38.067	13.8	42.142	15.2
1959.....	284.706	38.040	13.4	42.716	15.0

¹ Excludes guaranteed debt.

Representative WIDNALL. I would like to see whether, in relation to 2-, 4-, and 6-year periods, it has remained a fairly constant percentage.

Mr. MARTIN. Until recent years, I think it was a fairly constant percentage. In the past few years, there has been a gradual decline in it, but, on the whole, the programs have held up fairly well. One of the reasons for suggested action on the interest rate ceiling has been to reverse the recent trend.

Representative WIDNALL. To try to encourage that?

Mr. MARTIN. To try to encourage it.

Representative WIDNALL. Have you found an increased number of early cash-ins on series E-bonds? I know that many of the holders of series E-bonds acquire them through payroll deduction plans. Is there an early call for the money today as compared with 2 to 4 years ago, rather than holding them through the term?

Mr. MARTIN. I think some tendency toward early cash-ins during the last year or so has taken place in the larger denomination bonds.

Representative WIDNALL. That is, the people purchasing these bonds have not held on to them until maturity, which again poses a problem by way of refinancing.

Mr. MARTIN. That is right.

Representative WIDNALL. That is all, Mr. Chairman.

Representative PATMAN. Mr. Chairman, I notice that running throughout the report that the Federal Reserve and the Treasury made this kind of a statement which appeared on page 17 of your joint statement to Secretary Anderson.

Underlying the late spring speculative position of Government securities was a very low, absolute level of short-term interest rates as well as an unusually wide spread between the short term and long term market yields.

Then this statement goes on to say that this unusually wide spread vitally influences a shifting of market speculation, of further increases in Government bond prices.

In other words, you have got the bill rate down, but had not got the long-term rates down, so the amateurs at least thought that the long-term rate eventually would come down, or in other words that bond prices would go up.

Then your report also makes it clear that it was this unusually wide spread between the long-term rate and short-term rate that provided an incentive for the banks and nonfinancial corporations to enter into the repurchase agreements and buybacks that permitted so much speculation without any downpayment.

Is that correct, Mr. Martin?

Mr. MARTIN. I think that is about right; yes.

Representative PATMAN. Then let me ask this one, which I should perhaps ask one of the officials who made this investigation, perhaps, Mr. Roosa.

Was it generally true that the bond dealers and other professionals were misled by this unusually wide spread between the short-term and long-term rate, or was that just amateurs? What would be your answer to that, Mr. Roosa?

Mr. Roosa. I should make clear, sir, that I am not the best man to answer this, because at the time the incidents reached their peak, I was in Austria. But the evidence I have seen in participating in this study subsequently indicates to me that everyone active in the market was misled, or at least was misinterpreting the basic economic situation, for one length of time or another. It is the way in which markets are made up. Some people begin to see the path of the future a little sooner than others, and I suppose it is true that most of the dealers were fairly early in seeing what would lie ahead, and the implications of the changing business situation.

That is what they should do. That is their job, to be out in front of the market. Whether or not one could say that they were distinctly ahead of the many other highly competent financial observers who were engaged in trying to make judgments at this time, is very hard to say.

Representative PATMAN. That is the reason I am disappointed, because you did not get from the dealers the profit statements, Mr. Martin. In other words, I would like to find out if amateurs lost money as well as the other newcomers, or did just the big ones and the people who were in a better position to be in the know, whether they were or not, make money?

But of course, that is behind us. I still hope that those profit figures can be obtained.

How long had this kind of distortion between the bill rate and the long-term interest rate been developing? Had that been from the first of the year?

Mr. MARTIN. Yes; from November on, really.

Representative PATMAN. Could it have been avoided if the open market had not been operating under the bills-only policy?

Mr. MARTIN. In my judgment, no, Mr. Patman.

Representative PATMAN. On the whole, would you recommend a continuation of the bills-only policy?

Mr. MARTIN. Yes, I would. I have no hesitation on that. I think that it has worked well. I do not think it is perfect. I think we should continue to study it, and I welcome the observations that you and Mr. Reuss have made on it, and welcome your interest in it. I think we should continue to examine every aspect of it.

Representative PATMAN. What was the main problem in the recessionary period of the first half of 1958? Was it a falling-off in consumer spending, a drop in development, or what was it?

Mr. MARTIN. It was the liquidation of inventory and cutback in business investment.

The 1948-49, 1953-54, and 1957-58 recessions were each characterized by especially sharp inventory adjustments downward, though there were other factors of course.

Representative PATMAN. What would cause that? Was there any particular reason for that?

Mr. MARTIN. I think the falling off of demand and prices. Of course I happen to believe, Mr. Patman, that 1957-58 recession was a direct result of letting inflation get substantially ahead of us. When we had \$1 billion in gross national product, increasing every month, without any additional goods and services, it is a surprise to me that we did not have an adjustment sooner. I am awfully glad we pursued the policies we did during that time, because I think the adjustment would have been much more severe.

In 1958, during the first two quarters, there was a booming, long-term State and municipal market for securities.

Representative PATMAN. My next question bears on that.

During this period in the first half of 1958 that you are talking about, what were you trying to accomplish most by your monetary policy? Merely to prevent the inflation from getting worse, or to encourage investment, or what?

Mr. MARTIN. This is 1958, now?

Representative PATMAN. Yes, sir.

Mr. MARTIN. In 1958 inflation was not our problem as such. It was the preceding inflation that had led to the decline. We were doing everything we could to facilitate adjustments in the economy and help the economy stabilize for the recovery which has since occurred. The point I was making was that in the first half of 1958 we had this large expansion of State, municipal, and corporate spending projects through debt financing, many of which had been postponed, in my judgment, from the earlier period of tight money, and it was very fortunate that they came in at this time and acted as a stabilizing factor from the standpoint of both employment and adjustments.

Representative PATMAN. What did the Federal Reserve do for the purpose of trying to get long-term rates down? Do you feel you succeeded in getting long-term rates down?

Mr. MARTIN. Yes, I think they came down. They did not come down as much as I thought they would. The monetary developments from late 1957, when we reduced discount rates, to April, when the recovery was underway—we did not know it was underway in April, that is all hindsight now—were amazingly drastic. Talking about the money supply, money supply for several months in there was rising at the

rate of 8 percent and 12 percent, if you include time deposits in it. We were doing everything we could, so far as the money stream was concerned, to facilitate the stabilization of and assistance to the economy.

I think the bill rate got too low during that period. We cannot set these rates.

Representative PATMAN. Now, Mr. Martin, how do you reconcile the fight that you have been making against inflation with your support of the vault-cash bill, which reduced your power to deal with inflation, particularly with reference to the reserve requirements of the New York and Chicago banks, the Central Reserve city banks? In other words, that bill absolutely reduced your power to deal with inflation. How do you justify that and at the time that you are making such an earnest and sincere fight against inflation?

Mr. MARTIN. I would like to discuss that for a minute, Mr. Patman.

I have been up here testifying now for 8 years that I think, by and large, reserve requirements have been higher than necessary for the growth and development of the country.

Representative PATMAN. I am talking about the maximum requirements.

Mr. MARTIN. I am talking about that, too.

Let us go back to the period of the pegged market. One of the difficulties was that we decided that we could not use the general controls—open market operations and discount rates—but that we would have to mark up reserve requirements.

We marked up reserve requirements, and that put heavy pressure on the long-term market.

Representative PATMAN. When was that?

Mr. MARTIN. That was in 1950-51.

We put on so much pressure by marking up reserve requirements—at one point up to 20 percent—that in the period I am referring to, January of 1951, we literally destroyed our market for Government bonds. Bonds were being poured onto us, because we have no control over how the banks make their loans.

The fact that we tighten credit does not mean that the banks necessarily will deny credit to one of their principal customers. It may mean that if the demand for credit is strong, they will merely sell Government securities or some other securities out of their portfolio.

That was really the nub of what we were dealing with at the time of the Treasury-Federal Reserve accord.

When we went back to more orthodox methods and gave up the peg as such, we began to look at this problem in a broader perspective.

I think the growth that is ahead of this country is terrific. I am constantly testifying to that. I am a great bull on this country's future. If we will handle our finances soundly, we have an unlimited advance ahead of us.

We use the reserve requirement as a fulcrum for our monetary operation. I think that we should be moving toward lower reserve requirements.

The most difficult problem in the Federal Reserve is this matter of reserve requirements. I cannot get the people in the System to agree among themselves on it. I have given that up. And you will never get bankers or businessmen to agree on it. It looks simple, but it is not.

I wanted to do something on this in 1956. In 1955, in an exchange with you, I made some remarks along this line, and you said you hoped we would make a study.

We made a study. Then came the expansion in business. How do you account for what looks like a plan for a decrease in reserve requirements—the point you are making—when you have an inflation spreading as it was in 1956 and 1957? The answer is that we came up with this proposal in the recession, but Congress did not act on it then. It was held over until this year.

Representative PATMAN. May I interrupt there? You are not responding to my question. My question relates only to maximum requirements. In other words, you permitted the maximum reserve requirements to be reduced at a time when you were fighting inflation. I want to know why you were in favor of reducing your power to more adequately deal with inflation in the event that an emergency should arise.

I am talking about the maximum now, only.

Mr. MARTIN. In all of this type of thing the maximum cannot be completely divorced from the minimum; but I will tackle the maximum by saying we had some people that did not want to do anything with respect to the equalization of reserves. We were trying to get this together.

This has been called in some quarters an American Bankers Association bill. I asked the American Bankers Association to help us on it, and in 1954 and 1955 they worked on it. They did not go along with what we wanted, by any means, but we tried to work out a bill that we thought would be helpful to the longrun development of the country.

We have not lowered reserve requirements, and we do not know that we will lower reserve requirements at all in the next year.

Representative PATMAN. My time has expired, Mr. Martin, but I want to get back to you on that.

I believe Mr. Reuss comes next.

Representative REUSS. Mr. Chairman, there has been handed to me a release of July 24 from the office of Congressman Simpson, the chairman of the Republican Congressional Campaign Committee, which contains on pages 5 and 6 thereof a copy of the letter of Mr. Martin to Mr. Simpson of July 14, 1959, which I referred to before. I ask unanimous consent that Mr. Martin's letter be made a part of the record.

Representative PATMAN. Without objection it is so ordered.
(The letter referred to follows:)

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
OFFICE OF THE CHAIRMAN,
Washington, July 14, 1959.

HON. RICHARD M. SIMPSON,
House of Representatives,
Washington, D.C.

DEAR MR. SIMPSON: This response to the request contained in your letter of July 13 puts in writing the gist of the comments I made in the executive session meetings of the Ways and Means Committee on the amendments to the legislative proposals originally offered by the administration.

It is my considered judgment we are facing a serious financial situation. The limitation on interest rates is unrealistic in the light of present market quotations and denies the U.S. Treasury the tools essential to effective balanced handling of its borrowing needs. By statute the Treasury is now limited,

because of the ceilings, to the issue of short-term securities which under present conditions of rising prosperity is dangerous. These short-term obligations can readily be converted into money at the option of the holder. In effect, they are a substitute for money, and thus could swell the flow of money far beyond that needed to purchase available goods and services at current price levels. The threat of a money flow out of hand has a major impact on the cost of living and places a burden on all of us.

It serves no useful purpose at the moment to argue whose fault it is that we are in our present predicament. The fact of the matter is we are in it. The committee is not being asked to vote whether interest rates should or would go up or down, but merely to grant the Treasury authority to exercise its best judgment in meeting an existing problem. We are discussing a crucial matter—the credit of the United States. Failure to deal with this could (and I was careful not to threaten or assert that it necessarily would) have the most serious implications. It was my duty to warn of this, much as I disliked the task. These are the basic facts with which we were dealing and any amendments must be considered in this light.

The amendment to retain the statutory ceilings but permit them to be disregarded if the President found the national interest so required did not seem to me to present unworkable problems. Accordingly, I did not raise objections, although I prefer the original.

The "sense of the committee" amendment is quite a different matter. I object to this on principle. The Open Market Committee and the Federal Reserve Board are given the responsibility under the Federal Reserve Act for regulating the money supply. If the Congress wishes to spell out the means of doing this, it should amend the Federal Reserve Act and not tack this on to a debt management bill.

Furthermore, under present conditions, I am convinced that this amendment, when stripped of all technicalities, and regardless of whether the language is permissive or mandatory, will cause many thoughtful people, both at home and abroad, to question the will of our Government to manage its financial affairs without recourse to the printing press. To me this is a grave matter. We are here dealing with trust and confidence which is the keystone of sound currency. Therefore, I must oppose this proposal as vigorously as possible, as I did during the hearings.

The amendment limiting the President's authority to 2 years is, in my judgment, unsound. It could be a source of embarrassment to both the next President and the then Secretary of the Treasury.

I have tried as faithfully as possible to summarize what I actually said during the hearings, and not to introduce new ideas. May I, in conclusion, thank you and all the members of the committee for the courtesy and consideration shown me and my associates throughout the meetings. I am taking the liberty of sending a copy of this letter to Chairman Mills.

Sincerely yours,

WM. McC. MARTIN, Jr.

Representative REUSS. Mr. Martin, I am not going to take the time to read your entire letter at this time, but I would like to read the two paragraphs in which you address yourself to the so-called sense-of-Congress amendment, and I will read that to refresh your recollection. This is on page 6, about the fourth line:

I object to this sense-of-the-committee amendment on principle. The Open Market Committee and the Federal Reserve Board are given the responsibility under the Federal Reserve Act for regulating the money supply. If the Congress wishes to spell out the means of doing this, it should amend the Federal Reserve Act and not tack this on to a debt management bill.

There is one more paragraph, but I want to take this one up first. I take it that that first objection of yours is an objection in the realm of legislative tidiness, and that this first objection would disappear if the legislation enacted by Congress were an amendment to the Federal Reserve Act.

Mr. MARTIN. There is no question at all but that the Congress has the power to do what it wants.

Representative REUSS. But this first objection of yours, I gather, would be cured by proper labeling?

Mr. MARTIN. I want to make no mistake about it, though. I think it would be a mistake to do it, but that would be completely limited.

Representative REUSS. As far as objection No. 1 goes, that would be satisfied.

Mr. MARTIN. That is right.

Representative REUSS. Let us pass on, then, to objection No. 2, contained in your second paragraph:

Furthermore, under present conditions I am convinced that this amendment, when stripped of all technicalities, and regardless of whether the language is permissive or mandatory, will cause many thoughtful people both at home and abroad to question the will of our Government to manage its financial affairs without recourse to the printing press. To me this is a grave matter.

And I might interpolate it would be to me, too, if Congress directed you to get out the printing press.

We are here dealing with trust and confidence, which is the keystone of sound currency. Therefore, I must oppose this proposal as vigorously as possible, as I did during the hearings.

Now, let us address ourselves to objection No. 2, which we will call the psychological, metaphysical objection. That is, it is not related to anything within the four corners of the amendment. It is related to suspicions such as those Congressman Curtis voiced about the views on other subjects of certain of its authors. Would that be a fair statement?

Mr. MARTIN. As related to this matter, that is right.

Representative REUSS. Suppose the sense-of-Congress resolution, in the exact language in which I introduced it as House Concurrent Resolution 196 some months ago, and in the exact words in which I presented it to the Ways and Means Committee, and in the exact words in which it was adopted—and there is no difference of substance whatever in those three versions—were in fact passed by the Congress, suitably labeled as an amendment to the Federal Reserve Act so as to meet your point No. 1; suppose on the day that it passed and was signed by the President, a joint statement were made by the President, the Secretary of the Treasury, yourself, Majority Leader Johnson of the Senate, and Speaker Rayburn of the House, and suppose that you all said, "Congress has now passed the Ways and Means Committee bill with the amendment. We all want to make it clear that this resolution of Congress says absolutely nothing on the subject of whether the Federal Reserve Board and System should move faster or in a different manner than it has in the creation of additions to the money supply. All this resolution does is to criticize the Federal Reserve in two particulars and ask that they change their ways: First, when they do in their judgment increase the money supply, they should do so primarily, for the pendency of this bill, by purchase of U.S. securities rather than by further lowering of bank reserve requirements, as they have done for the last 6 years and as they say they intend to do in the future; and secondly, by amending its current-bills-only policy so that instead of an absolute prohibition on purchasing anything but short terms, except for the question of disorderly markets, there is a frame of mind on the part of the Federal Reserve whereby it is going to look at each purchase of U.S. securities on its merits and

not adopt any doctrinaire restrictions on its own freedom of action."

Suppose, then, that all the gentlemen I named, which includes yourself, were to make such a statement, would not such a statement mean that thoughtful people, both at home and abroad, could no longer question the will of the Government, that thoughtful people, with that statement before them, would not really think that the Government was about to turn on the printing press and become an engine of inflation? And would not thoughtful people then recognize that while a dispute still existed between the Federal Reserve and certain Congressmen and Senators about the quantum of money they are creating, nevertheless this resolution had nothing to do with that subject, but instead related to the two matters I have discussed: Namely, purchasing U.S. securities, and an end to the absolute nature of the bills-only policy?

Mr. MARTIN. And there would be an elimination of the use of reserve requirements during the foreseeable future.

Representative REUSS. Not an absolute elimination, but in the wording of the resolution, "Where feasible."

That is to say, the Federal Reserve would be given a broad hint by Congress that, barring special circumstances, it should act, when it acts, to create future additions to the money supply by the device of purchasing U.S. securities rather than by the device of so dealing with the reserve requirement feature as, on net balance, to increase the reserves that way.

But address yourself to the question which I am trying to put in a constructive and friendly way. What if we all got together for the good of the country and said, "Certainly not, there are no people around here who like inflation or want to have it, but at the same time, if one or the other of us had been a little bit doctrinaire and inflexible in the past, let us amend ourselves, consistent with a sound monetary policy."

Would that not be good for the souls of all concerned, and very good for the country?

Mr. MARTIN. Mr. Reuss, I think you have made quite a few "supposes" there, and done them very effectively. I think it is a matter of judgment and I am trying to give you my best judgment.

I think the nature of the financial problem that we are dealing with here is such that my statement is correct, that this would be the interpretation. I could be wrong on that.

Representative REUSS. But I am suggesting that we have this massive press conference with all you gentlemen explaining to the public.

Mr. MARTIN. Let me make the same statement about that that I have sometimes made about statements that are to reassure us on our gold or some other problem that seems to be under discussion.

Shakespeare put it very well once when he said, "Methinks thou protesteth too much."

I would think that if the President and the Secretary of the Treasury and all of us got together and made a statement of this sort, in the present atmosphere, the difficulties I have referred to would be increased rather than reversed. If the President, with all the problems he has, and the Secretary of the Treasury, with all the problems he has, were to cooperate and make that sort of a statement to the world, then if I were a thoughtful investor—maybe other investors

would not feel this way—but if I were a thoughtful investor, I would think, “This is a pretty serious matter, and it means that they are on the high road to inflation.”

Representative REUSS. And would your feeling be the same if this five-man symposium I am describing added to its statement: “The only reason we are making this statement is because there has been so much scare talk about what this resolution does, and so much misrepresentation of it, that really we think the record should be set straight. This is not a printing press amendment. It has nothing to do with the amount of the monetary supply. This is going to be left to the Federal Reserve as it always has been.”

Do you not think that would take the sting out of it?

Mr. MARTIN. No, I do not think you would cause people to think that your amendment is not inflationary and would help the Treasury. I sincerely believe the reverse. I think the amendment would be interpreted as inflationary, and it would not help the Treasury. Now you just have an honest difference of opinion.

Representative REUSS. That is not really the issue, though. The issue is whether this amendment is in fact inflationary, and you keep bringing in metaphysics, and hearsay, and what people abroad are saying or might say, although you have not really talked to them and are not sure what they would say. This is a little rough on me, because when I come back at you and say, “Why don’t you all get together and set the record straight,” you say, “Well, if we did that, people would think that we were really turning on the printing presses.”

That is a “heads I win, tails you lose” argument, Mr. Chairman.

Mr. MARTIN. I understand that. Let me just say that I have constantly thought about this for many years, and I am glad to see your interest in it, and I may turn out to be wrong on this, but money is a medium of exchange and a standard or store of value. But the realm of the metaphysics it gets into is in this confidence factor. There is trust and confidence involved, which is really the important factor. When that is displaced, then we are in trouble. That is the only way to express it; you may think it is mythical. There have been a lot of charges about talking too much about inflation, for example. Let me say I have only made one public address—back in December—in a long time, apart from the time I have been up here before Congress. Otherwise I have not said a thing.

Representative REUSS. I do not mean your talking about inflation. I am as much against it as you are. But I do frankly mind your stigmatizing the sense-of-Congress resolution which has been passed by the majority of the Ways and Means Committee as a method of turning on the printing presses. I think that keeps the metaphysics warm, so to speak, and I wish you would cool it off a bit and talk about the merits of it.

My time is up.

Mr. MARTIN. It is a source of regret to me that I have had to do that, because I was very careful not to make threats or to indicate where the end result of any of this would be, but as a trustee of the people’s money I have to give the best judgment I have. My judgment may be wrong, but I have to give the best judgment I have.

Representative REUSS. As I say, I cannot imagine a more inflammatory word than the word "printing press" money, and if anything scares the central bankers from New Delhi to The Hague, "printing press" does. I suggest a tidier terminology.

Representative PATMAN. Mr. Curtis.

Representative CURTIS. I yield momentarily to the gentleman from New Jersey for a comment.

Representative WIDNALL. I would like to make a comment on Mr. Reuss' "suppose, suppose, suppose" question. If it is necessary to call in all these people to explain the sense-of-Congress resolution and to bail Mr. Reuss out of this, why does he not withdraw the resolution or the amendment in the first place, and he can bail everybody out so we do not have to have a press conference?

Representative CURTIS. Mr. Chairman, I would like to read a comment from the Aubrey G. Langston & Co., Inc., newsletter of July 27, 1959. They are specialists in U.S. Government bonds and securities—which I think is very apt:

The somewhat tragic aspect of the matter is that the prolonged, somewhat acrimonious debate over a relatively simple matter is taken by people in other countries as a sign of the unwillingness of the Congress as a whole to take the steps that are necessary to maintain order in the Government's financial affairs and to preserve the future value of the dollar.

The issue before the Ways and Means Committee is a relatively simple matter; that is, whether or not the long-term bonds, which can only be sold under a ceiling of 4¼ percent can be sold unless this ceiling is removed.

That is the simple matter, plus, I might add, the E bonds, which many people have forgotten, which we likewise cannot market under their present interest ceiling. Because the law also includes an interest a ceiling on E bonds. Further, we have our problem of trying to encourage people to retain their holdings in long terms when they are about to come due. That is the third aspect of the bill. These all are relatively simple matters, and they are being cluttered up with something that is the subject of the complicated debate going on here and for 3 months on the floor of the House. The gentleman cannot even get it through his own committee, Banking and Currency, which has proper jurisdiction over it.

It is very obvious to me why the statement "the tragic aspect of the matter," is true. The simple situation, which has been presented to the Ways and Means Committee, should not be cluttered up with this kind of irrelevancy.

I yield to the gentleman.

Mr. CHAIRMAN. I yield back my time if he does not want to comment. There is one other thing I would like to say.

Representative REUSS. Yes; I will take the yield.

Representative CURTIS. Let me say this other thing first, though, before I do, because I should have said this.

In many respects I regret that this has come out in the Joint Economic Committee hearings, although in another sense I think it is good, because if we take a specific issue that is before us and direct these economic problems we have to that, we frequently begin talking about realities and get away from what we are apt to get into in this committee, too many generalities. But I do regret it has gone as far

as it has, because this should have been out of the way before this committee ever reached these hearings. It was planned and hoped that we would not have this subject of interest ceiling, which is still pending before the Congress, still pending at the time these hearings came about.

Yes; I yield to the gentleman.

Representative REUSS. Thank you.

Representative COFFIN. May I interject? This is what is called a high yield on a long-term issue.

Representative REUSS. I thank the gentleman for yielding. My wife frequently accuses me of clutter, but this is the first time a colleague has suggested I am guilty of the legislative variety of it.

I do not think this is cluttering up the bill. The Congress is asked by the administration to lift the $4\frac{1}{4}$ percent bond ceiling that we have had since 1918. Congress, it seems to me, is perfectly within its rights, and indeed is just doing its duty, if it says to the administration, "All right, we want to be responsible. We will go along and give you that necessary freedom of action, even though we wish we were not asked to do so. But in so doing, we want the administration, including the Federal Reserve, to do everything possible, consistent with a sound monetary policy, to make it unnecessary to go ever higher and higher in our interest rates, both on the national debt and, by percolation, throughout the entire economy."

The gentleman is, of course, within his rights in calling that clutter, but it seems to me good legislation for the Congress to pass out a package which not only says what we are willing to do, but gives the administration some guidance on how to do it.

Representative CURTIS. I might say to the gentleman that though that is the assumption, that the administration has not been doing everything it can to keep the interest rates down, and I believe they have, that is a fair subject for political debate.

Representative REUSS. Is it not also a fair subject for legislation by Congress?

Representative CURTIS. Certainly, probably so. But certainly not when we have an obvious thing which has to be done if we are to keep the interest rate as low as possible. We have to give the Treasury this flexibility. Otherwise you just force all the debt refinancing into the short terms. And, incidentally, this delay has already created great danger, because our recent issues have been above $4\frac{1}{4}$ percent. It is not that this is not subject matter for legislation, indeed, but we have a simple problem, relatively so, before the Ways and Means Committee which has to do with the Federal Reserve.

The gentleman is posing a very complicated problem on which many people disagree with his theory and his presumption that the Federal Reserve is not already doing what it can, within its ideas of the primary objective, which Congress has said is to preserve the value of money. And also this administration, I think, is trying to keep interest rates as low as possible.

Now I yield.

Representative REUSS. The gentleman makes quite a point of the inadequacy of the Ways and Means Committee to consider a complex subject matter. I certainly would not agree with him. I have a great respect not only for its jurisdiction, but for the capacity of its members.

Representative CURTIS. I do not want to yield when you make a statement of that nature. I have not indicated that the Ways and Means Committee is inadequate. I have indicated that the Ways and Means Committee has certain jurisdiction, and we do not have the background of having studied over a period of years the Federal Reserve Act, and the constant problems involved in the subject we are going into here; but the Banking and Currency Committee has. That is the point.

Representative REUSS. That is right, and I am on the Banking and Currency Committee.

Let me ask the gentleman, was not the witness, Chairman Martin, before the Ways and Means Committee on numerous occasions in connection with this bill?

Representative CURTIS. Of course.

Representative REUSS. How many different days was he up before you?

Representative CURTIS. Oh, my goodness, possibly 10.

Mr. MARTIN. Eleven days.

Representative REUSS. Would it be news to the gentleman if I told him that unless I am mistaken, Mr. Martin has not been before the Banking and Currency Committee at all this year?

I do not suggest this is any fault of Mr. Martin's. For one thing, you were ill for a time; secondly, you were not called as far as I know.

But Ways and Means had 11 times as much of the Federal Reserve as Banking and Currency has had. I will bet you do know something about this subject by now.

Representative CURTIS. Actually we could have had this interest ceiling bill out of the Ways and Means Committee in a day, as it should have been, if it had not been cluttered up with this matter.

I do remind the gentleman, inasmuch as this whole thing originated in a political atmosphere and as a result of some rather constant speeches on the floor of the House and the Senate accusing this administration of high interest rates, and so forth, that the gentleman's party does control the Congress, and they have the chairmanship of the Banking and Currency Committee and the majority members. If the gentleman's resolution had been in 2 months, as he said, why was it not brought out before Banking and Currency, and why was not a study made?

Representative REUSS. One reason is, we did not have a report from the Federal Reserve on it. But now we have had the benefit of their testimony before your committee.

Representative CURTIS. All I can say is, I think the statement of Mr. Langston is entirely accurate, that it is tragic, when we have a relatively simple matter before Ways and Means, which is so important to the fiscal integrity of this country, to have been horsing around as we have almost 2 months and causing damage even now by our failure to take action in these three simple areas: E bond interest rates, securities beyond 5 years, and this problem of trying to facilitate the holding of securities that have matured in the hands of the people that are the present holders.

It is those three areas in which we need the action; and this other thing, heaven knows what it might lead to and who is right or wrong on the thing. But the delay caused by not detecting it certainly is

causing damage now, and I hope the gentleman will, as the gentleman from New Jersey suggested, if it is going to require a massive press conference to clarify it, withdraw his resolution and let us get on with the debt management problem.

Mr. REUSS. The massive press conference would only be necessary because of misleading statements put out about what the resolution does.

Representative CURTIS. Oh, no. Let us say disagreement as to what it does. Let us not say "misleading." I happen to think the way we have described it is accurate. The gentleman is entitled to his interpretation.

Representative PATMAN. Mr. Coffin.

Representative COFFIN. Thank you, Mr. Chairman.

Mr. Martin, I do not know whether you or Mr. Roosa would be the one to comment on this question. I want to focus your attention on the condition of the market a year ago this spring with reference to the responsibility, if any, of the bills only policy for the situation in which we found ourselves.

In the statement you and Secretary Anderson gave us Friday, you say this:

Underlying the late spring speculative positioning of Government securities was a very low absolute level of short-term market interest rates, as well as an unusually wide spread between short- and long-term market yields. This low short-term rate level, together with the prevailing yield structure, vitally influenced the shaping of market expectations of further increases in Government bond prices. It further provided the incentives that led to unusual adaptations of customary credit instruments and terms, which facilitated a rapid swelling in the market's use of credit. This development made the market vulnerable to liquidation pressures.

Having said that, I would like to bring bills only into the picture to test the extent to which this policy was good or bad.

In the part of the country I come from, we like to use the water a lot, and I am not a yachtsman in a very large sense, but I like to row. I am never able to do very much when I row with only one oar. I am wondering whether rowing with one oar, namely, bills only, produced a result that was other than you would wish.

You make, in your statement today, three analyses of the intervention of the Federal Reserve in the Government securities market. Your first point was that when the Federal Reserve goes into the market you change the volume of reserves otherwise available to member banks.

My observation on this is that when you buy bills only, you are adding reserves to member banks and multiplying the credit available to these member banks, but the money made available, it would seem to me would be chiefly used by investors who would be presently in the short-term market and therefore would be looking for short-term securities in general.

Your second point, about the Federal Reserve's operations is that these operations affect the volume of the securities available. So when you go into bills only, you have stimulated a demand for short terms but, by your purchase, you have reduced the volume of short terms.

As to your third point, when you go into the short-term market and create by multiplying a demand for a lot more short-term securities which are not available in such great degree, the price goes down.

Did this not influence expectations that the long-term securities would go down also because of the shortness on the short-term market? And therefore, did not the policy of bills only, without any other oar to the boat, have quite a bit to do with the imbalance that finally resulted?

As I say, either you or Mr. Roosa might like to comment on it. Mr. MARTIN. I would like to let him comment on it also from his point of view.

Let me first say that there is more logic in the use of purchases of long-term securities when you are trying to stimulate expansion, in my judgment, than under present conditions. The long-term rate did go down at that time. It went down about a half of 1 percent. I thought it would go down more. I was wrong on it, but I thought it would go down.

We did not use only open market operations and reduction in discount rates because we made reductions in reserve requirements as part of our operation. We reduced the discount rate in November and then we reduced it three times subsequently, down to $1\frac{3}{4}$. We bought nearly \$2 billion of Government securities in the open market and we made three adjustments in reserve requirements also.

Representative COFFIN. That is multiplying the money available.

Mr. MARTIN. That is right.

It takes some time for lead or the lag. I cannot say positively that if we had bought some long-term Government securities—you made a very good point there—it might not have hastened a decline in the long end of the market. I have always conceded that.

However, that is a matter of judgment, and I think it is something we ought to bear in mind with respect to future operations. But on balance, I am not convinced that it would have substantially changed what happened, at least not to the point that we would have come out with a 100 percent better result.

Representative COFFIN. You are candid, because this is a little bit of a qualification of your earlier statement that if you had it all to do over again you would do exactly as you did.

Mr. MARTIN. Yes. I do not think you could ever say you would not change anything.

But what I am driving at is, for the matter of the broad approach to it, I do not know. In a manner of speaking, I think it would it would have been interesting if the recession had continued longer—I did not want it to do so, of course; do not misunderstand me.

Let us let Dr. Roosa comment on it. He may have a different point of view on this. All we want is the right answer to this problem.

Mr. Roosa. I think this is essentially the point: that as long as we are trying to study every situation with the best of all the combined judgment that we can put together, it must in the end become a problem of analysis and discussion among people whose careers are in his kind of work and who, if they make mistakes, make them because even with the accumulation of their experience, the problems are so complex that it will be impossible not to make a mistaken judgment once in a while.

Representative COFFIN. I agree with you.

Mr. Roosa. I just want to stress that there are no open-and-shut answers here.

I have tried very carefully to review the record last year. I suspect I came out a little differently from the position of Mr. Riefler, on my left, in this respect. I certainly do not know whether the view I have will prove to be right or wrong in full historical perspective. But the thing that makes it most difficult for me to reach a judgment on this situation has not been mentioned here. That is, that I believe—and please do not misunderstand me; I think this takes more explanation than I should presume to take time to elaborate fully here—that the level of long-term rates remained as high as it did because the Treasury was successfully offering more and more long-term issues through the spring period.

I also believe, sitting here now with the benefit of all the hindsight that that permits, that the result of that Treasury action was useful, that it prevented an excessive spreading of liquidity at a time when probably the System was putting in too much.

This only begins to shadow out the outlines of the broad question.

Representative COFFIN. What you have just said, though, would indicate that you might have some hindsight reflecting adversely on the use of bills-only in that spring. We have seen, if any analysis is correct, that this was an operation when the Federal Reserve did quite a bit to increase liquidity.

Mr. ROOSA. Yes, it did. The Treasury, on the other hand, was doing quite a bit to reduce liquidity. The net, as it emerged from this period—whether all was intentionally coordinated or whether some of the results may have been accidental—looking back on it now, I would say that as far as the combined effect of both operations is concerned, just about the right result was achieved.

Whether it would have been better if the Treasury had issued less long terms, I doubt. The fact that they were issuing them provided the offsetting pressure in the long-term market which avoided an undue seepage of liquidity through the economy that might otherwise have left us with a residue that would have been very hard to manage when the recovery came about, particularly because the recovery moved upward so fast. Nevertheless, trying to appraise that overall, I would say that for that situation we came out fairly well, and that the swing in the speculative market behavior that accentuated the actual turning point was one related more largely to excesses in financial practice. There are lessons in such experience that may have already been learned by those who were involved, but I think what happened is also going to have to lead to some changes in market behavior and perhaps in the flow of information. It seems to me that these are the major lessons of this period.

I do not mean to imply in this that I am in full agreement with everyone else in the System on the extent to which there may be some room for operations outside of the bill market. I do not think I am. But I feel that in the atmosphere of free discussion in which we engage in these matters, one person is sometimes bound to see things a little differently from the consensus. That has been my experience for some time.

Representative COFFIN. Are you at liberty to give your views as to the extent to which the Federal Reserve should go outside the bills market?

Mr. MARTIN. Mr. Roosa is at liberty to give his views on any subject.

Mr. ROOSA. I am at liberty; but the question relates to something that also is a very long and complicated story.

I would say, trying to shortcut detail and go into just a broad characterization, that I would probably be more likely in a given situation to come out in favor of a long-term operation than, for example, Mr. Riefler. But both of us would be considering it from all sides, quite freely. This is a matter to some extent just of differences in personal temperament. There are people in the System you can spot every time who are going to want to be easier in any situation, after appraising the facts, and others who are always going to want to be tighter, after appraising the same facts. I think it is a source of the richness and vitality of System thinking that we continue to have this strong representation of differing views and some differing biases or predispositions among the various people who participate in discussions of policy.

I have never had the feeling that if I felt strongly, if I were competent to express a view in a given situation—I am usually not well enough acquainted to do that—that I could not make whatever suggestion I wished, and that the consensus as it came through in the committee, of which of course I am not a member, but only an associate economist, would have taken that into account. I think that is all I could ask for.

Representative COFFIN. I just want to comment that that is a very fair statement, but it leaves me a little bit doubtful of our power to govern ourselves or to exercise conscious forethought, when Dr. Roosa said that during the last spring the Treasury went in one direction and the Federal Reserve went in another, and somehow it all came out right.

Mr. MARTIN. It sometimes happens in legislation, too, Mr. Coffin.

Representative COFFIN. I think it definitely does.

Representative PATMAN. Mr. Curtis.

Representative CURTIS. Thank you, Mr. Chairman.

In my interest in the other question there was one matter that I wanted to point out at this time that is contained in this material that is going to be sent to you, Mr. Martin, for your comment. I will not read the whole thing. It is really the tail end on which I want your answer. This is under the heading "The Appropriate Criterion or Criteria for Managing the Public Debt."

For some time now the Treasury has insisted that the issuance of long-term debt is essential to any anti-inflation program. The Treasury has largely failed in its attempt to lengthen the debt maturity, and yet it is this attempt as much as anything else which, for the difficulties it has had in managing its refunding and new money issues.

Of course, this is the staff posing this.

It would be well, therefore, to know the official rationale for this policy. Is it the ordinary rationale of countercyclical debt management policy, or something else?

That is not a question to you, because you could not comment on it officially.

In a word, what is it that is effected of this attempt to lengthen the maturity of debt, even in boom times? And is it likely that the expected benefits do in fact outweigh the costs involved? Might it not be better for the Treasury to follow a narrower policy of simply minimizing the cost, operating cost as well as in-

terest cost, of its debt operations, and leave to the Federal Reserve the task of keeping the right maturity mix in the market?

It is that last part I meant, but I had to read the whole thing in order for you to comment on it.

Mr. MARTIN. I think this is the basic question, and it is where the Treasury and the Federal Reserve come together. I am sorry that Senator Douglas is not here, because I usually make this comment to him. He has repeatedly said that "good fences make good neighbors," and I have repeatedly pointed out that in order to be good neighbors you have to have a revolving door to go through. I do not believe that you can completely isolate the joining of policy effectively.

The real problem, as I intimated earlier here, on short- and long-term securities is not so much the maturity distribution as it is to get the Treasury in a position where it can go to the market and get the best price that is available in the market at that time, and not be at the mercy of the market.

Representative CURTIS. In other words, to interpolate: not to have to go to the well so often, but to be able to have the debt coming up over a longer period of time.

Mr. MARTIN. That would unquestionably benefit them greatly. And also not to go to the well as a necessitous borrower.

Representative CURTIS. In other words, the posing of the problem by the staff does not include this very important aspect of the debt management which, in my judgment, has always been one of the basic reasons the Treasury has wanted to get more securities in long terms, and I might say in E bonds, too.

But now, as to the economic problem, where they say, "Is it the ordinary rational of countercyclical debt management policy, or something else?"—of course, it is countercyclical, in my judgment, but the real reason is not because it is countercyclical as much as it is because it is necessary in order to manage the debt.

But would you comment?

Mr. MARTIN. Yes. I think the Treasury's duty and obligation is to finance in the most effective way it can to save the taxpayer money. Our duty is to try to keep the money stream in such a way as not to interfere with their activities, but to accord with sound monetary policy.

There are times when those two come awfully close together, but it is perfectly clear to me that in times of expansion there are opportunities, perhaps, for given opportunities in which they can lengthen the debt. But the real problem that we are facing at the moment is that, lacking the tools, the proper tools of debt management, the Treasury has no choice.

Representative CURTIS. But to go to short term?

Mr. MARTIN. But to go to short term.

Representative CURTIS. Thank you, Mr. Chairman.

Representative PATMAN. Mr. Martin, would it be agreeable to you to answer any questions that the members submit to you in writing for the record?

Mr. MARTIN. Yes, indeed, sir.

Representative PATMAN. I want to ask you a question or two now about these reserve requirements. As you know, I have had some correspondence with you, and I do not have all the information I

desire. I sent you another letter. You probably received it this morning.

Mr. MARTIN. I got that letter this morning. I am sorry you did not think it was responsive.

Representative PATMAN. From the information I have from the best sources obtainable, I am convinced that the banks have never put more than a billion and a half dollars in the reserve fund, that is now \$18 billion. Does that conform to your thinking or not?

Mr. MARTIN. I do not know how you can separate what they put in.

Representative PATMAN. Here is the way it is done.

Mr. A. J. R. Smith wrote a very fine article on "The Sources and Uses of Member Bank Reserves, 1914-52," which is included in a pamphlet of the Federal Reserve Bank of New York, November 1953, entitled "Bank Reserves, Some Major Factors Affecting Them." Without objection, I will put that in the record.

(The article referred to follows:)

SOURCES AND USES OF MEMBER BANK RESERVES, 1914-52

(By A. J. R. Smith)

In 38 years of Federal Reserve System operations, the volume of member bank reserves has grown from roughly \$1.5 billion to nearly \$20 billion. What are the sources from which these reserves have been derived? What are the uses to which they have been put? And what are some of the major implications of this huge rise in the dollar volume of reserves for the operations and profits of the commercial banks and the Federal Reserve banks?

Is it correct to suggest, that, historically, as deposits have expanded, member banks have been forced to turn over vast sums to the Federal Reserve banks to meet reserve requirements, thus depriving the commercial banks themselves of funds that might otherwise have been put to profitable use? Would it be correct to go even further, to suggest that the holding of member bank reserves by the Federal Reserve banks has enlarged their potential earning power, at the expense of the commercial banks? Both suggestions seem plausible, especially from the viewpoint of an individual banker observing the direct effect of a given change in his bank's reserves. But the issues raised in these questions can best be answered by tracing through in detail the sources of reserves for the banking system as a whole.

Actually, the Federal Reserve banks have been the principal source from which the commercial banks have derived reserve funds since the founding of the Federal Reserve System in 1914. Under our fractional reserve banking structure, the Federal Reserve credit created by the Reserve banks has in effect, permitted commercial banks to effect a vast expansion in their loans and investments that otherwise would not have been possible. The extension of Federal Reserve credit has provided the commercial banks with the funds needed for meeting the mounting reserve requirements arising from the deposit expansion generated through the credit-creation process. Instead of levying a "tribute" from the commercial banks, the Federal Reserve banks have (mainly through their purchases of Government securities) provided the reserve base upon which a vastly enlarged balance of commercial bank loans, investments, and deposits has been erected over a period of nearly four decades.

Earnings as such have, for the most part, been of no immediate concern to the Federal Reserve banks. The System has generally brought about changes in member bank reserve balances as needed to provide an elastic money supply in conformity with the aim of furthering economic growth within a framework of economic stability, although twice it has had to provide the basis for abnormal expansions of bank credit for the financing of wars. On the whole, the earning assets of the Federal Reserve banks have tended to fluctuate inversely with the banking system's net acquisitions of reserves (loanable funds) from sources other than Federal Reserve credit. For example, at times when the commercial banks have obtained reserves from gold inflows, the Federal Reserve banks have often contracted their own earning assets as a partial offset to the increase in bank reserves resulting from the gold inflow. Thus,

when banks obtain reserves from other sources, the Federal Reserve System not only does not use the resulting growth of member bank reserve balances to finance a growth of its own earning assets, but instead it tends to reduce its earning assets. Growth in the earning assets of the Reserve banks has usually come about only when, for reasons of national economic policy, the System wished to provide additional reserves to the commercial banks.

AGGREGATE CHANGES FOR THE PERIOD AS A WHOLE

As the last column in the accompanying table indicates, net additions to the Nation's monetary gold stock and expansion of Federal Reserve credit have constituted the two principal sources of reserve funds over the period from the end of 1914 to the end of 1952. Net increases in the amount of currency in circulation and increases in the required reserves of the banks have constituted the two principal uses of these funds. The growth in required reserves of member banks resulted partly from statutory increases in the percentages of reserves which member banks have been required to maintain against their deposit liabilities, but mainly from the enormous expansion in bank credit and bank deposits that took place during this period.

When the Federal Reserve System was established in 1914, the total cash reserves (excluding interbank deposits) of all banks in the country, member and nonmember, were probably less than \$2 billion. During the 38 years from the beginning of 1915 to the end of 1952, the inflow of gold from abroad (together with some moderate amounts of domestically produced gold) contributed a net amount of more than \$21 billion to member bank reserves. The actual increase in U.S. gold stock, which also reflected revaluation of the dollar in 1934, was even greater, but approximately \$1 billion was still held as "free gold" by the Treasury at the end of 1952,¹ and about \$700 million was used as part of this country's subscription to the International Monetary Fund. Federal Reserve credit during this same period showed a net expansion of close to \$25 billion (almost entirely through purchases of Government securities), and Treasury operations, chiefly in the form of issues of "Treasury currency" (silver certificates and metal dollars, subsidiary silver, minor coins, etc.), contributed a relatively small additional amount, bringing the gross additions to member bank reserves to a total of over \$47 billion.

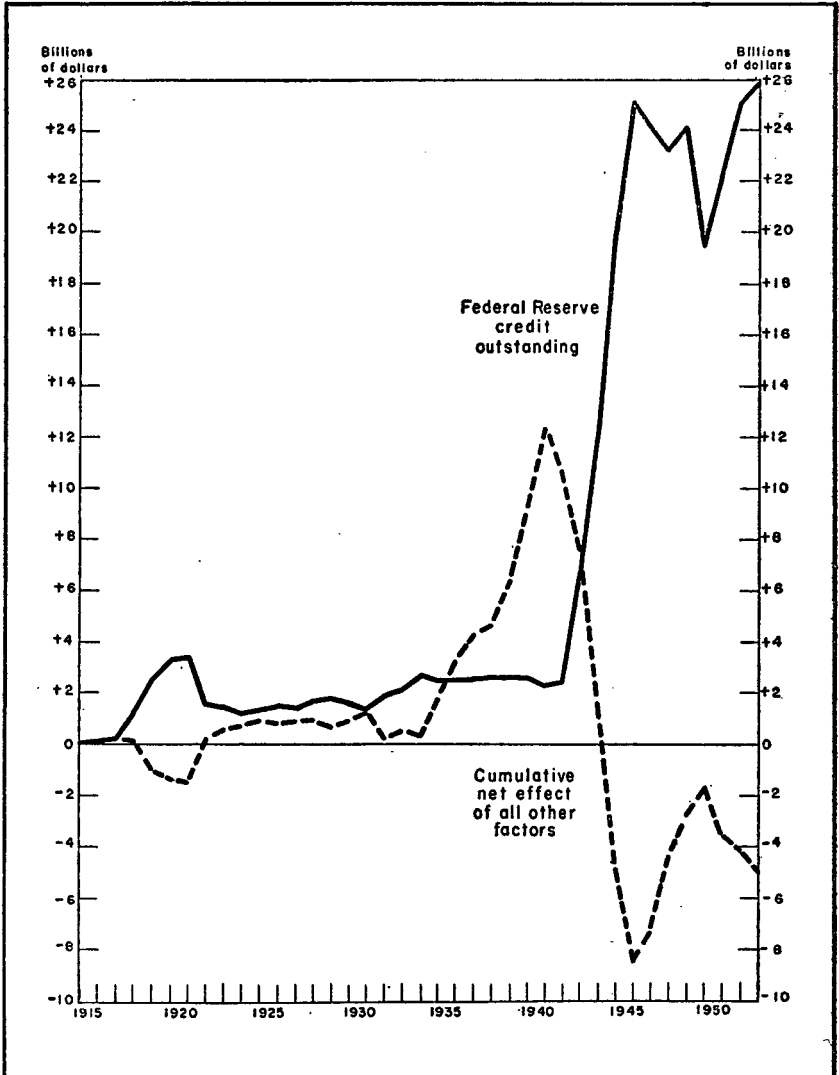
Over the same period, currency in circulation increased by more than \$27 billion, as banks obtained currency to meet the needs of their customers and to maintain adequate supplies of vault cash. Since the banks obtain this currency by drawing on their reserve accounts in the Federal Reserve banks, a corresponding amount of reserve funds was absorbed, leaving a net increase in member bank reserve balances of slightly under \$20 billion. Most of this increase in reserve balances was used as the basis for expansion of bank credit and was absorbed in increases in required reserves, leaving only a small residue to be added to excess reserves. The expansion in total loans and investments of member banks during this 38-year period was approximately \$111 billion, and total member bank deposits increased by \$139 billion.

From these summary data, it is clear that there could have been no such growth in the Nation's money supply—currency and bank deposits—or in the banks' earning assets, as has occurred without the great increase in Federal Reserve credit. While specific sources and uses of bank reserves cannot be precisely linked to each other, and while a given expansion in Federal Reserve credit has often provided banks with reserves to meet their currency drains, the fact remains that, from a purely accounting point of view, increases in reserves from sources other than the expansion in Federal Reserve credit between the end of 1914 and the end of 1952 did not supply member banks with enough reserves to meet the actual increase in the amount of currency outstanding. Thus, in effect, the banking system of this country, in order to do its part in financing this country's participation in two world wars and in providing the credit needed to finance the growth in the country's production and trade, has been dependent upon the ability of the Federal Reserve Banks to create additional reserve funds.

¹ In November 1953, \$500 million of "free gold" was used to retire Government securities in order to avoid exceeding the \$275 billion legal public debt limit.

FEDERAL RESERVE BANK OF NEW YORK

**Cumulative Changes in Federal Reserve Credit
and in All Other Factors* Affecting Bank Reserves, 1914-1952**



* "All other factors" includes such items as changes in gold stock, in foreign deposits with the Federal Reserve Banks, and in money in circulation.

RESERVE BANK EARNING ASSETS AND MEMBER BANK RESERVES

There have been periods in which the banks acquired large amounts of additional reserves independently of Federal Reserve credit. As mentioned above, the idea has been expressed from time to time that member banks, by depositing these reserve funds in the Federal Reserve banks, have enabled the Reserve banks to enlarge their earning assets and hence their earnings. This has led to the conclusion in some quarters that the earnings of Reserve banks have been derived from funds provided by the member banks, and hence that the member banks should be permitted to participate more largely in the earnings of the Reserve banks. On the basis of this conclusion, some observers have even contended that the payment of a large proportion of the Reserve banks' net earnings to the Treasury indirectly involves the subjection of member banks to a disproportionately heavy tax burden.

Changes in factors tending to increase (+) or decrease (-) member bank reserves and excess reserves, Dec. 31, 1914-Dec. 31, 1952

[In millions of dollars]

Factor	Dec. 11, 1914- Dec. 31, 1920	Dec. 11, 1920- Dec. 31, 1929	Dec. 31, 1929- Dec. 31, 1933	Dec. 31, 1933- Dec. 31, 1940	Dec. 31, 1940- Dec. 31, 1945	Dec. 31, 1945- Dec. 31, 1952	Dec. 31, 1914- Dec. 31, 1952
Treasury factors ¹	-335	+343	+239	² -1,510	+569	+2,078	+1,384
Gold and foreign account trans- actions.....	+1,108	+1,357	+41	² +16,830	-1,659	+3,433	+21,110
Currency in circulation.....	-2,293	+747	-941	-3,213	-19,783	-1,918	-27,401
Total.....	-1,520	+2,446	-660	+12,106	-20,870	+3,592	-4,906
Federal Reserve factors:							
Government securities.....	+287	+224	+1,926	-253	+22,078	+435	+24,697
Discounts, advances, and industrial loans ³	+2,937	-1,923	-793	-221	+241	-90	+151
Float ⁴	+119	-72	-28	+60	+498	+389	+966
Other deposits and Federal Reserve accounts ⁵	-262	-101	-71	-395	-58	-291	-1,178
Total.....	⁶ +3,036	-1,872	+1,034	-809	+22,759	+443	⁶ +24,591
Total reserves.....	+1,516	+574	37.4	+11,297	+1,839	+4,035	+19,685
Effects of changes in required reserves.....	⁷ -1,520	⁷ -668	+558	-5,541	-7,046	-6,063	-20,280
Excess reserves.....	⁷ -4	⁷ -94	+932	+5,756	-5,157	-2,028	-595

¹ Includes changes in Treasury currency outstanding, Treasury cash holdings, and Treasury deposits with the Federal Reserve banks.

² Under the Gold Reserve Act of 1934 the price of gold was increased from \$20.67 to \$35 per ounce; this resulted in an increase of approximately \$3,000,000,000 in the Nation's monetary gold stock and in Treasury cash. The effects of these changes have been included in the 1933-40 data shown here.

³ Changes in this total prior to 1934 consist almost exclusively of changes in bills discounted and bills bought; those during and after 1934 include changes in industrial loans; and those after 1939 consist mainly of changes in advances.

⁴ The volume of checks credited to the member banks' reserve accounts with the Reserve banks prior to actual collection.

⁵ Excludes foreign deposits. Federal Reserve accounts consist of capital accounts plus other liabilities and accrued dividends minus bank premises and other assets.

⁶ To make this total comparable with those for other periods shown, it has been adjusted downward by \$45,000,000. Such an adjustment has been necessitated by 2 features of member bank reserves in 1914: (1) member banks held some of their reserves outside the Federal Reserve banks; and (2) member bank reserve balances held with the Reserve banks were computed on a slightly different basis than in the later years shown in the table. See "Banking and Monetary Statistics," p. 327.

⁷ Estimated.

Note.—Because of rounding, figures do not necessarily add to totals.

The following review of various periods since the Federal Reserve System was established shows, however, that the earning assets of the Reserve banks have tended to decline at times when there have been large additions to member bank reserves from sources other than Federal Reserve credit—notably gold inflows—and have tended to be greatest when there have been heavy drains on member bank reserves from factors such as gold outflows and large public demands for currency. The ability of the Federal Reserve banks to add to the reserves of member banks by purchasing Government securities or by making loans to member banks stems, not from funds provided by the member banks, but

rather from the note issue privilege and the credit-creating power granted to the Federal Reserve banks by Congress. And, as the preceding summary of the sources and uses of reserve funds has demonstrated, the credit-granting capacity of member banks and the growth in their earnings over the entire period since the inauguration of the Federal Reserve System have been heavily dependent upon the reserves provided by the Reserve banks.

Indeed, the view that Federal Reserve banks invest the reserve deposits of their member banks in Government securities can now be seen to be the opposite of the actual process. What really happens is that, when the Reserve banks purchase Government securities in the open market, they create bank reserves. (The seller of the securities is given a check drawn on a Federal Reserve bank. He deposits the check in his bank. His bank then presents the check to the Reserve bank, and gets payment in the form of a credit to its reserve account.) Just as the commercial banking system of the country is able to expand deposits (through lending and investing operations) up to 5 times the amount of available reserves, if reserve requirements are assumed to average 20 percent, so the Federal Reserve banks can expand their own credit, that is, expand bank reserves, up to 4 times the amount of available gold certificates. Unlike the commercial banks, which will make use of excess reserves to expand their loans and investments if suitable opportunities are available, the Reserve banks do not base their decisions to lend or invest on the availability of profitable outlets for their funds. Indeed, at the end of 1952 the Reserve banks had close to \$10 billion of gold certificates in excess of the 25-percent reserve required against their note and deposit liabilities.

The misunderstanding with respect to this matter no doubt derives from the fact that individual member banks, except to the extent that they obtain reserves directly from the Reserve banks by borrowing, usually obtain new reserves through deposits with them by their customers of currency or checks drawn on other banks, or through sales of some of their securities. For the banking system as a whole, however, currency transactions with customers over the years have constituted an enormous drain on the banks' reserves, rather than a source of additional reserves, and the reserves obtained by one bank through collections of checks drawn on other banks involve only a shift of reserves between banks and cannot in any way add to the total volume of reserves. In fact, the deposits on which the checks are drawn are largely created through expansion of bank credit—bank loans and investments—and, as the deposits of the banking system as a whole increase, the required reserves of the banks correspondingly increase and the amount of free reserves is reduced. Sales of securities by the banks produce additional reserves only to the extent that the securities are purchased by the Reserve banks. To the extent that the securities are sold to bank depositors (nonbank buyers), there is a corresponding reduction in the banks' deposit liabilities, and, consequently, a fractional release of required reserves; but there is no overall increase in total reserves.

Finally, since the earning power of the Federal Reserve banks arises from the note issue and credit-granting authority given them by Congress, and since actual earnings are largely related to various functions performed in the national interest, the Reserve banks either have been legally obliged (from 1914 to 1932) or have considered it appropriate (from 1947 to date) to turn over a large proportion of their earnings (after expenses and the statutory dividend of 6 percent on their paid-up stock) to the U.S. Treasury.

WORLD WAR I AND THE INTERWAR YEARS

The sources of reserve funds and the demands for them varied widely from time to time over the 38-year period from the end of 1914 to the end of 1952. In the table, this period is broken down to show some of the major swings in the various factors affecting member bank reserves. The chart shows changes in Federal Reserve bank credit outstanding and cumulative movements in the banking system's net acquisitions and losses of reserves from sources other than Federal Reserve credit from 1914 to 1952 on an annual basis.

In the 6 years from the beginning of 1915 to the end of 1920, which covered most of the First World War and the postwar inflation, there was a net inflow of gold, which for those days was substantial. The public's demand for currency, however, exceeded the size of the gold inflow; consequently, the banking system suffered a heavy net loss of reserves. In addition, a rapid increase in the volume of bank credit occurred, first in connection with the financing of the war, and then to finance the postwar inflationary boom. As a result, there was a heavy

demand for Federal Reserve credit to provide the necessary reserve funds, which took the form mainly of member bank borrowings from the Reserve banks.

The next period, from the beginning of 1921 to the end of 1929, started with the postwar depression and ended with the "new era" boom. In that period a substantial gold inflow, together with a reduction in the amount of currency in circulation, provided the banks with a sizable volume of additional reserves. Part of these reserves was used as the basis for further credit expansion, but a major part was used (at the beginning of the period) to repay member bank indebtedness at the Reserve banks. For member banks, much of the period was one of high prosperity, but, despite an increase in member bank reserve deposits in the Reserve banks, the earning assets of the Reserve banks fell sharply and then remained at a relatively low level during most of the period, and the earnings of the Reserve banks were much reduced compared with the preceding period.

In the years of acute depression, 1930-33, the major factor affecting the reserves of member banks was the withdrawal of currency from banks by depositors who were disturbed by the wave of bank failures. An unprecedented liquidation of bank loans and investments released a substantial amount of reserves by lowering bank deposits and required reserves, but the banks nevertheless had to turn to the Reserve banks for assistance in meeting the demands on them. The Federal Reserve banks had supplied the banks with additional reserve funds at the end of 1929 and in 1930 through purchases of Government securities to assist the banks in reducing their indebtedness to the Reserve banks, and later in the period made additional security purchases in substantial amount to supply the banks with excess reserves and thus to make it easier for them to meet the cash demands of their customers.

The most important monetary and banking development of the period 1934-40 was the tremendous inflow of gold. It reflected, first, a flow of capital to the United States from the "gold bloc" countries which were endeavoring to remain on the gold standard without devaluation of their currencies and, subsequently, the flight of capital from Europe in fear of Nazi aggression before the war and payments for war materiel in the early stages of the Second World War. Despite some offsetting factors, such as a sizable increase in the amount of currency in circulation and a temporary sterilization of gold inflows by the Treasury in 1936-38, member banks were not only completely independent of the Federal Reserve System in maintaining their required reserves, but accumulated a very large volume of excess reserves for which they could find no suitable use. In that period, there was a steady expansion in member bank loans and investments, but competition for the available earning assets caused a decline in interest rates to unprecedentedly low levels, which had a depressing effect on the banks' earnings. At the same time, despite the extraordinary growth in member bank reserve deposits in the Reserve banks, the earning assets of the Reserve banks were at a very low ebb, and in some of the years their earnings were barely sufficient to cover expenses and statutory dividends. The increase in the Reserve banks' assets that paralleled the growth in their deposit and note liabilities was entirely in the form of claims on gold, which produce no earnings.

WORLD WAR II AND THE POSTWAR YEARS

During World War II, the excess reserves of member banks melted away rapidly as a result of the tremendous upsurge in public demands for currency. In addition, the reserves required of member banks increased rapidly (despite the suspension of reserve requirements against Treasury war loan deposit accounts in the banks), as a result of very large bank purchases of Government securities and the rise in private deposits as the Government spent the proceeds of the war loans. Furthermore, there was a sizable outflow of gold after 1942, reflecting heavy imports from other countries at a time when civilian production was restricted here and only very limited amounts of goods (apart from lend-lease operations) could be made available for export. As a result, there was a steep rise in the volume of Federal Reserve credit extended to enable the banks to meet both the drains on their reserves and their enlarged needs for required reserves as deposits increased rapidly. At the end of 1945 the amount of Federal Reserve credit outstanding was more than \$9 billion in excess of the total volume of member bank reserves.

Since the end of the war, there have been wide swings in the factors affecting the supply of reserve funds. The heavy gold inflow from the end of 1945 to the

fall of 1949, together with a gradual decline in the amount of currency in circulation after 1946 was nearly offset by the retirement of approximately \$6 billion of Federal Reserve credit. In effect, this retirement was accomplished mainly by the Treasury's use of its surplus receipts to retire Government securities held by the Federal Reserve banks. But at the low point in the fall of 1949 the volume of Federal Reserve credit outstanding still exceeded the total amount of member bank reserve balances. After the outbreak of war in Korea, a substantial outflow of gold, which reflected chiefly a great acceleration in U.S. imports, together with a renewed public demand for currency and a rapid increase in member bank reserve requirements as a result of loan expansion, brought about a renewed and very heavy demand for Federal Reserve credit. Despite the reluctance of the System to release a large volume of such credit in response to this demand, its support operations in the Government security market actually led to a growth in Federal Reserve credit which canceled the earlier postwar contraction. The March 1951 accord between the Treasury and the Federal Reserve System eliminated any System obligation to undertake open market operations to support Government bond prices. Nevertheless, additional small net purchases of Government securities were made during 1951 and 1952. Throughout the entire postwar period, therefore, the amount of Federal Reserve credit outstanding has substantially exceeded the total volume of member bank reserve balances.

The increase in currency circulation alone since 1940 has exceeded the total amount of reserves held by member banks at the beginning of the period by close to \$8 billion, and, in addition, the required reserves of the banks have increased by over \$13 billion, only a limited part of which is attributable to increases in percentage reserve requirements. Between the end of 1940 and the end of 1952, there were only relatively small net additions to bank reserve funds from sources other than Federal Reserve credit, so that the banking system has been dependent almost entirely upon expansion of Federal Reserve credit to meet its reserve needs.

These years have witnessed the greatest period of expansion in the history of banking in this country. Total loans and investments of all member banks increased by \$82 billion, and at the end of 1952 were well over three times their volume at the end of 1940. Gross earnings of the banks increased somewhat less than proportionately, however, and a considerable part of the increase which did occur was used to meet increased operating costs and heavier taxation. The direct benefit to bank stockholders in the form of dividends was limited; but there was a considerable increase in the value of their equity, as the banks retained substantial percentages of net profits to strengthen capital positions. Despite this plowing back of earnings, as well as some sales of new stock, however, many banks have had difficulty in increasing their capital funds in proportion to the growth in their business.

The rate of growth in the earnings (gross and net) of the Federal Reserve banks was much greater than that of the commercial banks during this decade, partly because their earning assets increased even more rapidly, partly because their expenses did not increase proportionately, and partly because the Reserve banks are not subject to income and profits taxes. As pointed out above, however, circumstances made it appropriate for them to pay the greater part of their net earnings to the Treasury.

Representative **PATMAN**. He goes ahead and discusses the sources of these reserves, how they were derived. At first, I know, the bank put in about a billion and a half dollars, most of it gold, I believe, at the beginning of the Federal Reserve. Since that time the facts indicate that the reserves have accumulated by reason of the inflow of gold or the purchase of securities by the Federal Reserve banks, principally.

What is your comment on that? Are you surprised that the amount would be so low, or do you dispute the fact that the amount as stated is correct, or to what extent is it incorrect?

Mr. **MARTIN**. The inflow of gold is certainly the bank putting it in, is it not, Mr. Patman?

Representative **PATMAN**. In a credit way; yes.

Mr. **MARTIN**. In an actual way.

Representative PATMAN. The banks did not themselves mine the gold and create the gold. They were just the beneficiaries of the inflow of the gold; is that not correct?

Mr. MARTIN. Yes; originally they had gold coin and currency.

Representative PATMAN. But I am talking about gold that comes into the country.

Mr. MARTIN. It comes in to a member bank.

Representative PATMAN. Yes; it does. It is paid for through the member bank. Of course the Treasury pays for it, I guess, by a check on the Federal Federal Reserve.

Mr. MARTIN. That is right.

Representative PATMAN. And the check then is deposited with the member bank. That is what you call his poured dollars, is it not?

Mr. MARTIN. That is what our Reserve System is.

Representative PATMAN. I am not disputing it. It is what you call his poured dollars. They get them without cost to themselves, do they not?

Mr. MARTIN. They are not getting it free.

Representative PATMAN. I did not say "free"; I said, "without cost to them."

Mr. MARTIN. They have a liability on their books as a result of it.

Representative PATMAN. Yes; that is right.

Mr. MARTIN. We put it into our statement.

I would be glad to try to go over this with you sometime.

Representative PATMAN. Fine. If you would answer it, I should be very glad to have the answer.

Some of our members could not be here this morning. Would it be satisfactory with you, Mr. Martin, to return here in 2 hours, at 2:30?

Mr. MARTIN. I will be here at 2:30.

Representative PATMAN. Very well, the committee stands recessed until 2:30 this afternoon.

(Whereupon, at 12:35 p.m., the committee recessed to reconvene at 2:30 the same afternoon.)

AFTER RECESS

[The Joint Committee reconvened at 2:30 p.m., Senator Paul H. Douglas (chairman) presiding.]

The CHAIRMAN. The committee will come to order.

FURTHER STATEMENT OF WILLIAM McCHESNEY MARTIN, CHAIRMAN, BOARD OF GOVERNORS, FEDERAL RESERVE SYSTEM

The CHAIRMAN. Mr. Martin, I regret that I was not able to be here this morning. By one of those strange coincidences, I had three hearings going on simultaneously. One committee was on lake diversion, which is a matter of some importance to my city. Another committee was dealing with the Housing Act and the question of whether or not we should try to override the veto of the President. Then there was this committee also in session.

I was unable to be here. I regret very much that I was unable to be here. I regret causing you to be back this afternoon. We appreciate your coming back, however, very much.

Mr. MARTIN. I understand perfectly, Senator.

The CHAIRMAN. I have been somewhat distressed at the talk which has come from high official quarters of the danger of inflation. The President and his advisers have indulged in such talk. I am not certain that the Secretary of the Treasury has. I know you have made statements from time to time expressing your fear of inflation and, indeed, implying that inflation was present and upon us.

I know that this has been referred to with the best of intentions. I do not want to have you think that I am questioning the purity of your intentions. But the effect of all this talk of inflation, of course, is to send down the value of Government bonds with a resultant increase in yield, and, hence, to create a higher interest rate in Government securities, which is then a justification for higher rates on new issues.

In addition to this, it helps to promote a change in the market and sends up the price of stock at the same time that it decreases the market price of Government bonds.

If inflation is here, of course, we should face it, because no policy should be contrary to the facts. I remember, however, that when Senator Fulbright launched his investigation into stock market prices some years ago, he was subjected to a very vigorous attack by the then Secretary of the Treasury, Mr. Humphrey, on the ground that he was sending down the prices of stocks.

I want to make it clear that I am not making such an attack upon you. But I do think that the effect of what I personally would call scare talk has been most unfortunate in sending down the price of bonds, sending up the interest rates, sending up the price of stocks.

In view of all of this, I wondered if I might not review with you the recent movement of both the cost of living index and the wholesale price index, which are found on pages 23 and 24 of the Economic Indicators for the current month.

I wonder if you or your staff have copies of the Indicators here? I will ask the members of our staff to have ready the charts relative to this.

These figures only go to June, but in terms of consumer prices they show an index of 123.7 for June of 1958, an index of 124.5 for June 1959, an increase of only eight-tenths of 1 percent in a year, and five-tenths of this occurred in 1 month, May-June 1959.

The explanation of the Bureau of Labor Statistics was that this was largely seasonal, and would be offset later in the summer. If you examine the items where the increases have occurred, you will find that in the field of medical care, for instance, the increase in that year has been from 144.2 to 150.6. In the field of personal care, the increase has been from 128.6 to 131.1.

In the case of other goods and services, it is from 127.2 to 129.2. In housing, or perhaps we should say rent, 137.7 to 139.5. In other words, the increase during this period has been very, very slight, and such increase as has occurred has been in the field of services rather than the field of commodities.

If you turn to page 24 of the Indicators—"Wholesale Prices"—you will find that in June 1958, there it had been 119.2 and on July 14, 1959, 119.5. In other words, the wholesale index rose by only 0.3 during this year.

These, I think, are facts that should be kept in the foreground. I well remember 6 months ago you testified before us that you thought there was a tremendous amount of latent inflation inside the economic system, which would probably break out at any moment.

I would like to ask this question: In view of what has happened, can you really say that there has been inflation during this last year?

Mr. MARTIN. I do not have any hesitation of saying so, Senator. Let me try to put it this way, Senator:

I have been coming up here now for about 8 years, and in almost every appearance that I have made up here, someone has raised the same point that you are raising. Yet we all know what has happened to the dollar in that period. These movements are explosive in their force; and while, thank goodness, there has been no precise movement against the dollar during this period, we have been working very strenuously, the Treasury and ourselves, so far as the financial aspects of this are concerned, to see to it that the boat is not rocked inflation-wise.

The CHAIRMAN. Do you take the credit for the stability of prices, then?

Mr. MARTIN. I take some of the credit.

The CHAIRMAN. Then do you think the danger of inflation has largely departed?

Mr. MARTIN. Not the slightest. I think this, Senator: That for the first time in late 1955 and 1956, as you and I discussed it then, I saw the expectation of inflation beginning to get ahead of us. I am not engaging in scare talk, I am just trying to keep the problem in focus, and I now find that the elevator boys and too many other people around the country are more interested in common stocks as the way to riches than they are in fixed-income investment. I think that is a very serious and unfortunate national development.

The CHAIRMAN. I think it is, too, and I think one of the factors which has made them more interested in common stocks than bonds has been this talk about the inevitability of inflation, that the danger has been blown up out of all correspondence to reality, and the result has been to frighten the American people about bonds as long-term investments, and, therefore, by talk you have helped create, with the best will in the world, some of the problems with which you now try to deal.

Mr. MARTIN. Senator, I take a little different point of view. I have been sorry that I did not do more talking in 1956 and 1957 than I did.

The CHAIRMAN. We are now talking about 1959.

Mr. MARTIN. Unfortunately, as I keep trying to emphasize, inflation is a process, a very insidious process, that has been going on since the war, and once you get people into the frame of mind—to put it the way the Secretary of the Treasury put it, I thought very aptly, where it is safe to speculate and not safe to invest, then you are in a very dangerous situation, indeed. I believe that the trend has been in that direction.

The CHAIRMAN. There was an upward movement of prices in 1950 and 1951. The Senator from Illinois not only recognized that, but tried to deal with it.

Not all of my brethren agree with me, but I think some part of the driving force for the accord of 1951 came from the Senator from

Illinois. At that time, the distinguished Chairman of the Federal Reserve Board was Assistant Secretary of the Treasury, which was very much—"which"; I did not say "who"—was very much opposed at the time to the policy of the accord, and which had to be forced into the accord with a club.

So the Senator from Illinois can claim that he is no summer soldier or sunshine patriot in this matter. But at the same time he does not believe in playing up dangers which at the moment are non-existent.

If you will furthermore look at this chart on the board, you will find that consumer prices were substantially steady in 1952, 1953, 1954, 1955, and only began to move up in 1956 and 1957, and in the first part of 1958, and since then have been steady.

I think you will further find that the increases which took place in 1956, 1957, the first part of 1958, were primarily in the fields of durable goods, where the control of output was in the hands of a relatively small number of companies, and where, therefore, price agreements between producers were very dominant factors.

I think it would be very hard to maintain the contention that the increase in prices in these years was due to an expansion in the circulating medium greater than the increase in physical products, because I think all the evidence is to the contrary. We can submit data on that.

Mr. MARTIN. Senator, I would like to put into the record the figures that have just been placed in front of me.

In the 12-month period we have had \$8½ billion of inflation in our gross national product. I don't think that is a negligible amount, \$8½ billion of inflation in the 12-month period. In the past three months, the inflation in gross national product, annual rate has been \$1 billion a month.

I am referring here to GNP in current dollars from the second quarter of 1958 to the second quarter of 1959 compared with GNP in constant dollars as reported in the latest edition of Economic Indicators.

The CHAIRMAN. During that period you had a revival of business activity which required more money to float the goods at a constant price level.

Mr. MARTIN. That has all been taken into account in these figures.

The CHAIRMAN. It certainly did not show up in the price index.

Mr. MARTIN. The Consumers' Price Index has only recently begun to rise. But we were having some rather interesting price developments in the first half of 1955, for example, when we were having stability in our price index, achieved at that time by a decline in farm prices with an increase in durable goods prices. That is not the sort of stability we are looking for.

The CHAIRMAN. You say the inflation has only recently begun to show up in the field of prices. It is true there was the May to June increase in the cost-of-living index. However, I think the Bureau of Labor Statistics says it is primarily seasonal and will largely disappear when the food commodities come on the market in the fall.

But if you turn to page 24 of the indicator, you will find the index of wholesale prices, which is much more sensitive than the cost-of-living index, showed 120 for April of this year and 119.3 for July 14

of this year, or actually decreased nearly 1 percent in the 3 months. So there has been that indication.

I think that is shown by the chart on the easel.

Mr. MARTIN. Other than farm products on this chart on page 24, we have 125.3, I think, in May of 1958 and 128.2 in the week ended July 14. There was a decline in farm prices during that period from 95 to 88.3.

I think that is a significant move that has to be watched. I also want to caution you again on these statistics that we have to use as guides; they are not conclusive in themselves.

The CHAIRMAN. I notice they are always quoted when they are in your favor, but disparaged when against you.

Mr. MARTIN. No; I try not to do that, Senator.

The CHAIRMAN. My time is virtually up. I wanted to depart temporarily with you on this note: If you examine the Consumer Price Index, you will find that the increases have been entirely, I think one can say, in the field of services.

Mr. MARTIN. Largely; that is right.

The CHAIRMAN. Almost entirely. And in building. These administered prices which do not lend themselves readily to the quantity theory of monetary explanation, these certainly cannot be explained with the quantity theory of money.

I believe one of your eminent advisers in a candid moment before another committee of the Senate said that credit control could not deal effectively with the problem of administered prices. You cannot control hospitals or the American Medical Association, can you, by rigid credit control?

Are not these price factors something which come up from the bottom rather than being controlled from the top? Do you remember the old controversy which went on when I was a graduate student between Prof. Lawrence Laughlin, who was head of the department at my university at Chicago, and Prof. Irving Fisher at Yale, and at the time Laughlin was thought to be absurd because he was insisting on the importance of individual prices and Fisher was insisting merely on the global totals?

I thought he was foolish at the time, but with the passage of years, and the facts brought forth by some of your eminent staff, I have come to the conclusion that there was a great deal to it, and you cannot control the cost of medical services and those other items by credit control.

I think even in the field of durable goods certainly there are price agreements. I have no doubt but that there are price agreements in steel, cement, and other things. You are whistling in the wind, almost, when you try to control those perfectly by credit controls.

Mr. MARTIN. I have always recognized the limitations of credit controls.

The CHAIRMAN. This is fine. Now we are getting somewhere. This means that we should seek supplementary sources of price controls and not confine ourselves purely to credit controls.

My time is up. I will recognize my general and good friend, the Senator from Connecticut.

Senator BUSH. Mr. Chairman, I will say to the Governor I am sorry I was not here this morning because we had a conflict with the

housing hearings. I had to be there along with my good friend from Illinois.

The CHAIRMAN. We each watched each other.

Senator BUSH. Yes. I had to be there to watch him.

He has said, the chairman has spoken earlier, about the scare talk having had an effect upon the price of Government bonds. I would like to observe with regard to that that I do not believe that the scare talk, which he calls the scare talk, has had any material effect on the price of Government bonds.

I think what has had the effect have been events that have taken place which have been noticed by intelligent investors and people who make opinions and make markets, so to speak, and cause things to happen. This includes not only the important economists and observers in this country, but also in other countries, and it includes not only the financial institutions in this country, like the insurance companies and the pension funds and the investors of other people's money, but it also includes the central banks of the world, who watch the figures and the developments, and are able to interpret them and analyze them.

They do not pay too much attention as to what the politicians say about the situation. I would like to ask you if you agree with that observation or not.

Mr. MARTIN. Yes; I agree with that, Senator. I think scare talk is never good. But scare talk has not been what has caused the decline in Government bonds at the present time.

Senator BUSH. I agree that scare talk is an undesirable thing. But if we are going to stop the sources of inflation, if we are going to stop the sources of deterioration of the credit of this Government, we have to talk about it, unfortunately; we have to talk about the things that are undermining the credit of the Government, if we are going to correct them.

The only way you can correct them is by action at the source of the trouble. I don't see how it is possible in a Government like ours, in this kind of a government, for us to avoid talking frankly about our problems, because otherwise I do not believe we would ever get anything done about them.

The political pressures in favor of inflationary measures are at times so great that I simply don't believe that we can avoid talking about them and avoid talking about the possible consequences of them. So I venture to express the hope, although I do not believe it is needed, that the Chairman of the Federal Reserve Board and his colleagues, members of the staff who have made many fine analytical statements in the last year or so dealing with this whole subject, will continue to point out the cause of the real trouble, the roots of the evil, so that the informed opinion, in and out of the Congress, may be able to see what the real trouble is.

I have no questions, Mr. Chairman.

Mr. MARTIN. May I interject one thing there, Senator?

The CHAIRMAN. Of course.

Mr. MARTIN. Just for the record, I have only made one formal talk outside of my appearances in the Congress on this subject. That was last December.

The CHAIRMAN. Your appearances here have been quite interesting in nature.

Mr. MARTIN. I made it last December. As I explained to you, Senator, at the time of our February hearings, when you graciously permitted me to, I did that after a great deal of soul searching and with the conviction that it was in the public interest.

The CHAIRMAN. I am sure you thought it was in the public interest. Congressman Patman?

Representative PATMAN. Mr. Martin, I do not want the impression to get out from these hearings that the whole dispute is over the Reuss amendment, as fine as the amendment is on the Ways and Means Committee bill; that we are not opposed to the 4¼ percent increase. I am. I am for his amendment. I would like to vote for the amendment and vote against the increase.

Mr. MARTIN. I think I understand your position.

Representative PATMAN. I feel that if you cannot keep short-term interest rates down, you certainly will not keep long-term interest rate down. Whenever you have an administration that started over 6 years ago, determined to raise interest rates, and raise them more and more and more, and you have a Federal Reserve Board cooperating to the extent that they have not one time raised reserve requirement, I feel as if they are getting along too well together in what I consider to be against the people in raising interest rates to a very high level.

For that reason, when I have an opportunity to vote to stop it, I am going to vote to stop it. I just feel like the interest rates would go on up and up, and if we have to pay high interest rates, let's pay them on short-term obligations, so we can get rid of them quicker.

If we take the lid off now, and you issue 6- and 7- and 8-percent bonds, 30 and 40 years, it is a long time before we would get rid of them. But if you have to issue 6-, 7-, and 8-percent bonds, let's do it for just as short a period of time as possible. That is my feeling about it.

Considering the Reuss amendment to the Ways and Means Committee bill, I don't see why you would object to that when you did not object to the qualification that was put on in the conference report on the vault cash bill. It occurs to me that that restricts the Federal Reserve about as much as Mr. Reuss' amendment would on the Ways and Means Committee bill.

Mr. MARTIN. Do you mean changing from 20 to 22 percent—the upper limit?

Representative PATMAN. No; I am talking about the qualification that was put on by the conferees, to the effect that it is not the intention of the Congress, to encourage or cause the Open Market Committee to reduce its holdings of U.S. Government securities.

In other words, we have put a sense of Congress resolution in there, and I didn't hear of the Federal Reserve objecting to that.

Mr. MARTIN. I was not familiar with that as a sense of the Congress amendment, Mr. Patman. Maybe I was asleep at the switch, but I didn't so understand it or interpret it.

Representative PATMAN. You do not understand that the Congress endorsed the policy of the Federal Reserve transferring any of your bonds to the private banks, do you, in the passage of the so-called vault cash amendment?

Mr. MARTIN. We have never had such a policy. Let me point out on the reserve requirements—

Representative PATMAN. I am not talking about policy. I am talking about doing it separately, collectively, or any other way.

Mr. MARTIN. Well, I make no bones of the fact that I would like to see the banking system, as such, handle the decisions with respect to advancing credit to customers or not advancing credit to customers. That is their primary purpose and objective.

I want to see the banks do that in the maximum way consistent with the growth and development of this country. Therefore, I think reserve requirements are too high.

Representative PATMAN. Relate that to your holdings of U.S. Government securities.

Mr. MARTIN. Our holdings of U.S. Government securities are not maintained for the purpose of making money, or for the purpose of trying to benefit the Treasury indirectly by those holdings. We are making our adjustments in the money market through the holdings of Government securities, and we wish that the debt were smaller and we didn't have so many of them outstanding.

But we are making those adjustments with respect to the flow of money, and not with respect to whether it benefits the banks or benefits the Treasury.

Representative PATMAN. I thoroughly understand your position on it, Mr. Martin, but I think that this morning, when you talked about working with the American Bankers Association on a bill, I do not think you can deny that the American Bankers Association had in mind getting a bill through Congress that would authorize or permit or encourage the Federal Reserve authorities to transfer about \$15 billion of those bonds that you now hold in the private commercial banks. You cannot deny that, can you?

Mr. MARTIN. Well, I don't know what was in the mind of the American Bankers Association in working on the bill. But there was no—

Representative PATMAN. It was in writing, Mr. Martin.

Mr. MARTIN. Well, as I said this morning, I did what I could to stimulate the American Bankers Association to make the study on reserves. I sincerely believe that the reserve requirement level has, by and large, been too high for the growth and development of the country that I foresee. We did not follow the American Bankers Association recommendations.

Representative PATMAN. I could not understand why you would. You had a fine weapon there. Just like if you were an apple knocker, and you had a long stick, and you could reach the apples at the top of the tree, then you would agree to have the stick cut half in two so you could not knock the apples.

I cannot understand it. You had reserve requirements to where you could increase those reserves to 26 percent if you needed to, if an emergency should exist. You agreed to cut that stick off.

Mr. MARTIN. Mr. Patman, you and I discussed this many times. I don't honestly see—I have tried awfully hard to get this point on raising reserve requirements. Under present conditions, if we raise reserve requirements, we would just knock the bottom out of the Government securities market and interest rates would go, in my judgment, considerably higher than they have been.

I do not see how they could help but go that way. If banks have a choice between making a loan to a good customer or selling a Government security or another security in their portfolio to meet a reserve requirement, they are going to take it.

Representative PATMAN. How can you know so much about it when you haven't tried it? Every time you have used the weapon that would increase the interest rates of the bank, every time.

I do not know of a time when there has been conflict of interest between the public in low interest rates and the banks in high interest rates that the Reserve System has not taken the side of the banks.

Mr. MARTIN. Well, let me salute Senator Douglas—

The CHAIRMAN. Don't start anything between Congressman Patman and myself.

Mr. MARTIN. I want to point out—and I am quite serious on this—that I watched, and I may not have observed correctly, but I watched when I was Assistant Secretary of the Treasury what increases in reserve requirements under a pegged market did to the Government securities market.

They came pouring in at par and 22/32 because we raised reserve requirements from 18 to 20, from 20 to 22, from 22 to 24 percent, and the demand for credit was such that ultimately we had to find a device for placing over \$15 billion of those bonds with insurance companies and others at a more attractive rate.

Representative PATMAN. Mr. Martin, that is not comparable at all, in my book.

Mr. MARTIN. Well, it is my experience.

Representative PATMAN. I still say that every time you sought to tighten credit you kept on raising interest rates and have not tried raising reserve requirements, so you cannot be an expert on that.

Mr. MARTIN. Let's take the recent times.

Representative PATMAN. 1951 was the last time you raised reserve requirements.

Mr. MARTIN. I am not denying that. But you said reduce interest rates. I am pointing out that in 1957 we did everything in our power to ease money properly, judiciously, and effectively.

Representative PATMAN. It was not very effective.

The CHAIRMAN. Would the gentleman yield?

Representative PATMAN. Certainly.

The CHAIRMAN. Isn't it true that in the periods of recession you have always lowered reserve requirements, and during periods of revival you have always increased interest rates, so that the method which you chose has always been the most profitable one to the bankers?

Mr. MARTIN. The only place I question is that we have not increased interest price. The demand for credit is such—

The CHAIRMAN. You have no power over interest rates?

Mr. MARTIN. We have an influence on interest rates, but we cannot control them, sir.

The CHAIRMAN. You influence them?

Mr. MARTIN. Yes.

The CHAIRMAN. Your influence, then, in periods of revival have been thrown on the side of increasing interest rates.

Mr. MARTIN. That has been the trend. I have used the—

The CHAIRMAN. If the influence has been thrown on the side of increasing interest rates and your influence operates, then you have increased interest rates indirectly.

Mr. MARTIN. We have permitted the forces of the market to operate; we have not obstructed the forces of the market.

The CHAIRMAN. You merely reflect the market?

Mr. MARTIN. In large degree that is true.

The CHAIRMAN. I always thought that the Federal Reserve claimed as one of its influences, the effect on interest rates. Now I learn you don't have any effect.

Mr. MARTIN. The Federal Reserve is certainly not all-powerful.

The CHAIRMAN. I don't say you are all-powerful. I simply ask if you are somewhat powerful.

Mr. MARTIN. We have some influence.

The CHAIRMAN. And some influence on interest rates?

Mr. MARTIN. Yes.

The CHAIRMAN. So in periods of revival, you help to raise interest rates?

Mr. MARTIN. We try not to obstruct.

The CHAIRMAN. Doesn't the record show that in all periods of revival you have influenced interest rates? Haven't you raised the rediscount rate?

Mr. MARTIN. Yes.

The CHAIRMAN. And this has had an effect on the general interest rates. Then in periods of recession, what you do is lower the reserve ratios. I have time and again put into the record the history of the reserve ratios. I think the record abundantly bears me out. I will do it again if necessary at this time.

I will ask that it be included at this point in the record, to point out that whenever there is a recession, you lower the reserve ratio, so in one case you increase the multiplier and the other case you increase the multiplicand.

The result is always greater so far as bank earnings are concerned than it otherwise would be.

(The information referred to follows:)

Member bank reserve requirements

[Percent of deposits]

Effective date of change	Net demand deposits ¹			Time deposits	
	Central reserve city banks	Reserve city banks	Country banks	Central reserve and reserve city banks	Country banks
1917—June 21.....	13	10	7	3	3
1936—Aug. 16.....	19½	15	10½	4½	4½
1937—Mar. 1.....	22¾	17½	12¼	5¼	5¼
May 1.....	26	20	14	6	6
1938—Apr. 16.....	22¾	17½	12	5	5
1941—Nov. 1.....	26	20	14	6	6
1942—Aug. 20.....	24	20	14	6	6
Sept. 14.....	22	-----	-----	-----	-----
Oct. 3.....	20	-----	-----	-----	-----
1948—Feb. 27.....	22	-----	-----	-----	-----
June 11.....	24	-----	-----	-----	-----
Sept. 16, 24 ²	26	22	16	7½	7½
1949—May 1, 5 ²	24	21	15	7	7
June 30, July 1 ²	-----	20	14	6	6
Aug. 1, 11 ²	23½	19½	13	5	5
Aug. 16, 18 ²	23	19	12	-----	5
Aug. 25.....	22½	18½	-----	-----	-----
Sept. 1.....	22	18	-----	-----	-----
1951—Jan. 11, 16 ²	23	19	13	6	6
Jan. 25, Feb. 1 ²	24	20	14	-----	-----
1953—July 1, 9 ²	22	19	13	-----	-----
1954—June 16, 24 ²	21	-----	-----	5	5
July 29, Aug. 1 ²	20	18	12	-----	-----
1958—Feb. 27, Mar. 1 ²	19½	17½	11½	-----	-----
Mar. 20, Apr. 1 ²	19	17	11	-----	-----
Apr. 17.....	18½	-----	-----	-----	-----
Apr. 24.....	18	16½	-----	-----	-----
In effect July 1, 1959.....	18	16½	11	5	5
Present legal requirements:	-----	-----	-----	-----	-----
Minimum.....	13	10	7	3	3
Maximum.....	26	20	14	6	6

¹ Demand deposits subject to reserve requirements which, beginning Aug. 23, 1935, have been total demand deposits minus cash items in process of collection and demand balances due from domestic banks (also minus war loan and series E bond accounts during the period Apr. 13, 1943, to June 30, 1947).

² 1st-of-month or mid-month dates are changes at country banks, and other dates (usually Thursday) are at central reserve or reserve city banks.

Source: Federal Reserve Bulletin, July 1959.

Mr. MARTIN. That has been true from the period of about 1958 to date, where the gold inflow and outflow has not been of a nature to cause reserve requirements to have the uses to which they were put earlier. I don't know that we may have a return of that. If we had a heavy inflow of gold at the present time, I wouldn't hesitate to raise reserve requirements quickly.

The CHAIRMAN. In other words, there is some other reason.

Mr. MARTIN. That is our problem. The difficulty is to take periods and project a continuation over any lengthy period of time of conditions.

The CHAIRMAN. I think the record goes back to 1953, with the coming of the new administration into power, and not merely 1956.

Representative PATMAN. They reduced it with the coming of the new administration and have never raised it.

The CHAIRMAN. That is what I am saying. The record goes back to 1953.

Mr. MARTIN. It goes back to 1951, for that.

Representative PATMAN. Have you completed?

The CHAIRMAN. Yes; I have; and I apologize to Congressman Patman.

Representative PATMAN. You mentioned this morning how helpless the Secretary of the Treasury is, going to the money market hat in hand. He would be very helpless indeed were it not for the fact that he has another agency of Government right there with him, the Federal Reserve, which has money-creating power and the power to manage and control monetary matters, and could help the Secretary of the Treasury if the Federal Reserve only wanted to.

I have studied the operations of the different central banks of the world. I don't know too much about them, just a smattering knowledge of them, but I don't know of a single country where they have a central bank where that central bank does not come to the aid and rescue of its parent, the Government. I don't know of a single one except the United States of America. I don't think it is a very happy situation for the Federal Reserve to sit idly by and permit interest rates to go clear out of sight, which are so burdensome, extortionist interest rates on the people, and permit the Secretary of the Treasury to be so helpless and futile in his efforts to get money by passing the hat.

I just can't understand our great Federal Reserve System.

You refuse to support the Government bond market at 2½ percent. You refuse to support it at 3 percent. Maybe you had good reasons for it and maybe you were wrong, and the rest of us were wrong. You refused to support it at 3½ percent. You refused to support it at 4 percent. Now you refuse to support it at 4¼ percent.

When are you going to support it? Will you support it at 5 percent? Will you support it at 6 percent? Will you support it at 7 percent?

Mr. MARTIN. I hope that we will never support it and that the Treasury of the United States will never be so weak that it has to rely on the central bank to justify its existence.

Representative PATMAN. Now you justify your existence. Here you are serving the Congress. I assume you still recognize that. You know, one time Mr. Walcott and you were talking about it.

Mr. MARTIN. I would prefer to use trustee rather than servant; but I will not object to being called a servant.

Representative PATMAN. Then you were saying you were a servant, and we discussed it on that basis, and we finally agreed upon the principle of agent. But regardless of that, you are subservient to the Congress, and you should carry out its will, and yet you are against this "sense of Congress" resolution.

Another thing I cannot understand is why you, as an agent of Congress, or using any phrase or any definition you want of your subservience to the Congress—which you concede—go to the Executive and try to get the Executive to go against your master, the Congress. That is on the 4¼-percent amendment.

Mr. MARTIN. Mr. Patman, I have no influence over the Executive. I have very little influence over anybody.

Representative PATMAN. You recommended to him and he accepted it, didn't you?

Mr. MARTIN. I made no different statement to the President than I made to the Ways and Means Committee and that I made to you, that as a trustee for the Nation's finances—under a trust indenture given by the Congress—I want to discharge my duty to the best of my ability.

Representative PATMAN. So far as the money is concerned, Mr. Martin, I asked you about these reserves. I think people are willing for banks to expand their reserves under the Reserve System. I am strong for it. Whether it is 7 to 1 like it is, across the board, or whether it is 10 to 1 in certain banks, or 20 to 1 on time deposits. But if I am correct about the reserves and the member banks, we are not only permitting an expansion of 10 to 1 and 20 to 1, but we are permitting an expansion of \$100 to \$1.

Here is what I base that on: Starting with the Federal Reserve System when the member banks put in their gold and their money, and the way I have arrived at that amount, the banks have only put in a billion and a half dollars and they have withdrawn most of that.

But we will suppose they have it in there. The rest of that has been obtained through the inflow of gold and through the purchase of U.S. Government securities. That \$16 billion that is listed now as reserves of member banks was not paid in by the banks at all. It is by reason of reduction of requirements in some cases—of course, that didn't increase the amount—the inflow of gold at the purchase of U.S. Government securities by the Federal Reserve banks.

If the commercial banks only have a billion and a half dollars invested and they have much less than that, they have already made loans and investments equal to \$150 billion. So that is \$100 to \$1.

I am awaiting your reply to my letter, Mr. Martin, and the question that I asked you to deny what I have just said. I think you will verify that.

Mr. MARTIN. Mr. Patman, as I said to you this morning, we will take another look at your letter, and I will try to segregate these items out. I am not able at the moment to follow your reasoning on it.

The CHAIRMAN. Congressman Reuss.

Representative REUSS. Mr. Chairman, I would like to talk a little bit about elevator boys. I noticed in your colloquy with the chairman you said that you thought that one of the troubles with the U.S. securities market was that elevator boys have gone into the stock market. I have not myself conducted any depth studies or motivation researches concerning elevator boys, though I do know quite a few.

I commend this to you for study, seriously: I suspect that elevator boys, who have gone into the stock market a good deal recently, have not done so at the expense of the U.S. securities market. I suggest that they have not really held U.S. securities in any large amounts.

I suspect they have gone into the stock market because it is boiling, and it looks like a chance to make an attractive short-term capital gain. I suggest that the real decimation among the holders of U.S. securities has been among much more conventional and stolid holders, the financial intermediaries, savings and loan associations, pension

trusts, mutual savings banks, and so on, and that it really will not do to say that the trouble with the U.S. securities market is that speculators, through fear of inflation, have gone off into the stock market. I suggest that a lot of the newcomers to the stock market are people who weren't holders of U.S. securities at all; furthermore, that a lot of the former holders of U.S. securities, particularly the intermediaries, are still in fixed income securities, indicating that they are not afraid of inflation.

But somehow or other they are afraid of something that is wrong with the U.S. securities market. One of the things, I think, that is present in their minds, is that there are such crashing losses to be taken in a U.S. security that you buy in June, let us say, at \$100, and before your eyes it dwindles down to a market value of around 90 in just a very few months.

This, at least, is my reading of part of it. I know you will study that view.

Mr. MARTIN. Let me exonerate the elevator boys. I was just using that as a term.

Representative REUSS. We all know and admire many fine elevator boys, and they, as well as everybody else, have entered the stock market.

Let me refer you, Mr. Chairman, to page 40 of your annual report, released on July 24, 1959. That describes the bills-only policy, and t here, on page 40, it says:

Operations for the system account in the open market, other than repurchase agreements, shall be confined to short-term securities.

It then goes on to say that that was the unanimous formulation of the Open Market Committee, with the exception of one man, Mr. Hayes, the Vice Chairman.

I might say if I had been on the Open Market Committee, there would have been two.

Mr. Hayes stated, so it says, that he would vote to approve the statement if the qualifying phrase, "As a general rule" were inserted after the word "shall."

However, poor Mr. Hayes was not successful, and the qualification was not permitted.

Now I find to my delight that Hayes has triumphed, apparently, because in this morning's statement to us, in speaking of the bills only policy, you say, Mr. Chairman:

The practice or technique—
of bills only—

was adopted not as an iron rule but as a general procedure for the conduct of current operations.

I hope that is right. I hope that this does indicate a departure from the iron quality of the existing rule. I hope it represents a future intention, as of today, of the Federal Reserve to treat these matters on their own merits and to see whether in a particular case, it can best carry out its function by purchasing bills, notes, certificates, or bonds, whichever is most appropriate.

That is precisely what the sense-of-Congress resolution expresses the hope that you will do.

Without asking you to comment unless you want to, I will let the record speak for itself. It does seem to me that Mr. Hayes' position, which I think was wholesome as of March 4, 1958, has now prevailed.

I do not ask you to comment, but you may, if you wish.

Mr. MARTIN. I will be glad to say this: What we try to do is reflect accurately in these reports the discussion. Sometimes it is a difficult thing to do. The matter of words in connection with this was discussed at great length in the Open Market Committee, and the consensus was against Mr. Hayes as to the value of making the change that he wished to make.

But there was no disagreement in the Committee that it was not an ironclad rule that would never be departed from. It was a question of whether the wording would be changed in his way—in the way that he was suggesting would be more effective in enunciating that principle.

Representative REUSS. Let the commentators take a look at the language of the Open Market Committee and the language of what you said this morning, and see what the words mean.

Mr. MARTIN. We will be very glad to.

Representative REUSS. Am I right in my impression, Mr. Chairman, that this week the Federal Reserve acquired some \$2.6 billion of long-term—that is, 4 years, 8 months—U.S. Treasury securities?

Mr. MARTIN. In the course of an exchange, that is correct. We held over \$8 billion of these, and we put around \$5.5 billion of them into the 1-year securities and \$2.6 billion into the 4-year-9-month securities.

Representative REUSS. You had \$8 billion of short terms and in your trade you came out with some short terms but with \$2.6 billion of long terms, 4 years, 8 months?

Mr. MARTIN. Yes. A short time ago we did that in splitting up another issue. I don't remember exactly what date it was.

Representative REUSS. Did the world come to an end when you did that?

Mr. MARTIN. Not the slightest.

Representative REUSS. No flight of gold from this country?

Mr. MARTIN. I haven't seen any yet.

Representative REUSS. No flipping of lids by international money authorities in New Delhi or Hong Kong?

Mr. MARTIN. I haven't seen any.

Representative REUSS. I am sure there wasn't, because it seems to me a perfectly sensible thing. Again, just what Congress in its modest, diffident hat-in-hand way is asking you to consider. Therefore, I suggest to you that on this bills-only matter, when you get right down to it, when you take what you did last week, when we let your deeds speak, and when we let your words speak as they spoke this morning, really you shouldn't set so much store about a bills-only policy, because it turns out that upon occasion you depart from it.

Mr. MARTIN. Well, Mr. Reuss, that is the point we have been trying to make right along. We have never set such store by the bills-only policy. It is not an end-all. On your amendment, we have set considerable store about being able to use reserve requirements in the flexible way which we would be precluded from doing under your resolution, and we have also set a good bit of store by the fact that the context in which this has been presented is one that implies

criticism of the Federal Reserve—that the Federal Reserve brought on the predicament that we are in, by virtue of our actions. I don't think that is justified or correct.

The so-called bills-only policy is a technical procedural matter. We have Open Market meetings every 3 weeks, and any member of the Committee can raise it at any time for review or in connection with the Treasury issue. I cleared with the Open Market Committee with respect to this particular issue you are talking about, and they gave unanimous consent to it.

Representative REUSS. You will admit that \$2.6 billion of long-term bonds is a lot of bonds for a bills-only buyer to buy?

Mr. MARTIN. Well, let us try to get this straight. For one thing, we said short-term securities. We never said short bills only.

Representative REUSS. Is a 4-year 8-month security a short-term security?

Mr. MARTIN. Well, I would call that a relatively short-term security. What do you think of in terms of short-term securities, 60- and 90-day bills?

Representative REUSS. I think 4-year 8-month is at least an intermediate term security. After it is a little older than that, it gets to be a long-term security. But if you are going to define everything as short-term securities, which might be one way out of this, then you and I have it made.

Mr. MARTIN. We have said preferably short-term securities. The wording which you read was quite correct in our report. We said short-term securities, excepting disorderly conditions.

Representative REUSS. But there was nothing disorderly last week when you bought \$2.6 billion.

Mr. MARTIN. This was in the exchange operation.

Representative REUSS. I know, but you acquired them.

Mr. MARTIN. Certainly we acquired them for the purpose of evening out the maturity distribution. That was exactly the reason we did it for, for the maturity distribution. But we were not actually purchasing them in the market, which is an altogether different thing.

Representative REUSS. I wish you would explain the difference, monetarily speaking, between acquiring \$2.6 billion of 4-year 8-month securities in the open market, and acquiring them, de novo, from the Treasury.

In either case you have \$2.6 billion.

Mr. MARTIN. We end up with \$2.6 billion. But there is quite a difference when we hold securities and exchange them. There is quite a difference, even, when we have bills and they run off, although the monetary achievements may be the same. And there is a difference when you actually go into the market and solicit bids and offers. There is that distinction, and that is an important distinction to us.

Representative REUSS. From what you just said, I gather, then, that your objection to the so-called Reuss amendment is not with respect to the idea of no doctrinaire adherence to a bills-only policy—such as some people have said you have been following, but I am delighted to hear you have not been—but that your objection is to the advice that you should proceed by purchasing U.S. securities, rather than by further lowering bank reserve requirements.

Mr. MARTIN. I think that gets to the purpose of the Federal Reserve Act as I read it today. Whether you say purchasing U.S. securities of varying maturities, I think as far as my approach to this is concerned that the proper way to do that, which we discussed this morning, would be to change the Federal Reserve Act, and spell it out. I would hope that you wouldn't do it, because I think we need all the latitude we can get. As I indicated this morning, however, Congress has the power; I have no question whatever about that.

Representative REUSS. I see my time is up, Mr. Chairman.

The CHAIRMAN. Congressman Curtis.

Representative CURTIS. I have just one comment.

Of course, the context in which the Reuss amendment must be taken is in reference to a definition on long-term and short-term securities because the ceiling is only on securities 5 years and over. Is that not correct?

Mr. MARTIN. That is correct.

Representative CURTIS. And for that reason, most people have been referring to securities below 5 years as short term and those above 5 years as long term.

The gentleman from Wisconsin is familiar with that. For that reason, he was in error in referring to the 4 years 8 months as a long-term security.

Representative REUSS. If you will yield for a half minute, perhaps we can straighten this out now.

If I was in error, I want to be the first to admit it.

Is it the definition of the Federal Reserve System that short-term securities, as used by the bills-only policy and as solemnly set forward on page 40 of the annual report, refers to securities of 10 years or less, 8 years or less? When does a short term become an intermediate term?

Mr. MARTIN. Let us not have any misunderstanding on this. Mostly we talk about short-term securities, and we are talking about 1 year or less. This 4¾ is an exception on that basis. But the point Mr. Curtis is making is that the interest ceiling applies to 5 years and longer.

Representative REUSS. But that has nothing to do with the point of whether you violated your bills-only philosophy by buying the longer terms.

Mr. MARTIN. I will agree with that.

Representative CURTIS. The point I was making is that the Reuss amendment is in context with a bill that has to do with securities of 5 years and over, where there is a ceiling, and the ceiling does not apply to securities below 5 years. Because of that context, I think it tends to create an erroneous impression to refer to something under 5 years as a long-term security, simply because of another context. I think Mr. Martin has now fully clarified the definition. Maybe we need a third term of intermediate.

Representative REUSS. Again, we will have to await the publication of the printed record to see whether it is clarified. It certainly is not as far as I am concerned. I don't know whether the bills-only policy applies to securities of 2, 3, 4, 5 years, or whether it doesn't.

Representative CURTIS. If I may say, the gentleman—

Mr. MARTIN. I wish I could get you, Mr. Reuss, to refer to it as short-term securities instead of bills only.

Representative REUSS. How do you define a short-term security?

Mr. MARTIN. I said, generally speaking, a year or less.

Representative REUSS. What about when we aren't generally speaking? Is it anything over that? Can you have a short term of more than a year? Words must mean something.

Mr. MARTIN. Supposing we didn't have anything in our portfolio. The next shortest would be 18 months, let us say.

Representative REUSS. I would say get together the Open Market Committee and amend the short-term securities policy forthwith.

Mr. MARTIN. Since we meet every 3 weeks, I think we can readily decide what to do.

Representative CURTIS. If I may take some of my time back, I would like to point out that Mr. Reuss has been referring to two different things, and he switches. One is, of course, the bills only policy, and in that relation. I suggest that probably short term and long term mean one thing.

But the second thing he has been addressing his remarks to has been the bill before the ways and means which has to do with the moving of interest rates on securities beyond 5 years.

In that context, short-term and long-term securities have a different meaning. It has usually been the breaking point of what the interest ceiling applies to and what it doesn't. I have tried to interpose to clarify that.

The CHAIRMAN. The questioning by Congressman Reuss has not been deducted from your time, Mr. Curtis.

Representative CURTIS. No, I had the opportunity to question this morning.

The CHAIRMAN. Mr. Coffin.

Representative COFFIN. Mr. Martin, I wonder if this year, in the circumstances in which we find ourselves with the practice of the Fed coming in and buying 90-day paper, you are not making rather a problem for the Treasury—that is, constantly in the fix of trying to replenish this very short-term paper.

I am wondering if over the next months or the next year it would not be wise—and this does not get into the debate on bills only—if it would not be wise to have the Fed buy some issues that are of 12 months' duration or 18, or 24 months; at least not as a permanent thing but to ease this situation during this fairly critical time.

Mr. MARTIN. It might be desirable, but the real problem at the moment is that we probably should be selling securities, not buying. We are not worried at the moment with too easy a situation as such.

You see, we have to try to look at this thing in terms—well, I am not forecasting policy now. We have a great many factors, the steel strike and other things now, and stabilization in the economy. We just do not know.

But the Treasury has been adding, of course, to the supply of bills inordinately recently. In the last week, we had \$19 billion of new Treasury issues; \$5 billion of cash and \$14 billion refunding, and \$5 billion of the total went into bills.

Representative COFFIN. I am just wondering about the concentration on the bills, whether there has to be a choice between raising the interest rate on your bonds on the one hand, or continuing as you are at the present time and for the past substantial period of time,

or whether there is not a middle course where you could be of great assistance to the Treasury by operating in the market with these 12- or 18-month issues.

Mr. MARTIN. If it were consistent with policy we certainly would not hesitate to do that. But the point I am trying to make is that, at the moment, it is not my problem.

Representative COFFIN. To change the subject a little bit, has the Federal Reserve made any studies on the impact of interest rates on various sectors of the economy?

I would want to know before voting for an increase in interest rates what sectors would be affected as opposed to what sectors would be affected by a tax increase. In either case it is taking money out of people.

Have you made any studies to indicate what the impact will be?

Mr. MARTIN. We have been engaged in a very extensive study of small business the first parts of which we presented to the Banking and Currency Committees and Small Business Committees, and we are now presently gathering material on the last scheduled part of it. We hope it will be ready before too long. It won't be ready for the next 2 months.

Representative COFFIN. That would be one important area, certainly.

Mr. MARTIN. Our thinking so far has been that the impact of interest rates, increase in interest rates, generally falls on the marginal side, whether he is a small man, medium-sized man, or little man.

Representative COFFIN. You say small, medium sized, or little?

Mr. MARTIN. Large; I am sorry. I misspoke myself.

I meant large instead of little.

Representative COFFIN. I did not know there were any big marginal people. I thought you were quite correct when you said small, medium, and little.

Mr. MARTIN. I think there are some large enterprises that have marginal activities.

If it is a question of getting financed, they may be forced to defer it as interest rates tighten up.

Representative COFFIN. What about impact on State and local governments? Do you have studies on that? Or would that be in the context of the studies you say you are now engaged in?

Mr. MARTIN. We have been doing a lot of work on that. I pointed out earlier this morning that one of the sustaining things in my judgment in the 1958 recovery was the fact that a great many State and municipal securities that had been deferred because of the higher levels of interest rates in 1957, came in the market with a vengeance in January, February, and March of 1958, which was one of the largest extensions of that type of credit in history. I think it was a very important sustaining force in laying the groundwork for the present upward swing for which we are all grateful and appreciative.

Representative COFFIN. How broad would this study be, of the impact of interest rates on the sectors of the economy?

Would there be other fields than small business?

Mr. MARTIN. I will ask Mr. Young, the head of our division of research, to reply to that question.

Mr. YOUNG. This is a very difficult kind of study. We are always engaged in trying to determine from what information there is available and to develop new information that will throw some light on the different sectors and the degree to which they are affected.

I do not believe that any really definitive information will ever be developed that we can have available from time to time. Small pieces of information that would seem to add up can help in getting insight into the difficult problem of just what the effect of these credit developments may be.

Representative COFFIN. We can raise interest rates and it does not have such public clamor. Although there is plenty of that, it would not have half the clamor of a tax increase. And yet it is the exaction of money from many sectors.

Mr. YOUNG. That is right.

Representative COFFIN. I would hope that we would have a fair amount of at least generalized information available when we come to face this.

Mr. MARTIN. We want to get it. Of course, with increases in interest rates, where increased interest is a profit to the saver as well as a cost to the borrower, there is an impact on the economy you would never get from a tax increase.

Representative COFFIN. It is useful though to see who they are.

Mr. MARTIN. Exactly.

Representative COFFIN. It is not purely economical?

Mr. MARTIN. That is right.

Representative COFFIN. I have just one other question, Mr. Martin, in the field of your testimony that has not been touched as yet.

That is the part that is not directly addressed to monetary theory, but the last part of your statement where you indicated that you had revised the index of growth and had found that we were 10 points higher than we thought we were.

Does this mean that our production over these past 2 years has been better than we thought?

Mr. MARTIN. Yes, that is right. I will ask Mr. Young to comment on the index because he has worked on it.

Mr. YOUNG. Of course, the revision at the higher level comes about by our being unable, on the basis of the information that was earlier available, to take into account all the gains that were in fact there.

Representative COFFIN. Yes, but this changes our whole figures on the product.

Mr. YOUNG. That is right.

Representative COFFIN. Does it also change the conclusions we have hitherto reached regarding the productivity increase?

Mr. YOUNG. This will have some considerable impact on our motions of productivity gains over the period.

Representative COFFIN. So the productivity over the past 10 years will appear somewhat better than hitherto?

Mr. YOUNG. That is correct.

The CHAIRMAN. Will you yield?

Representative COFFIN. Yes.

The CHAIRMAN. May I ask if this increase in productivity is due to an improvement in your basic data, or to a change in your weighting system?

Mr. YOUNG. It is due in part to a change in the weighting system because we are now able to include electric power as fuel.

The CHAIRMAN. Is there involved in this the question of values as of an end year which gave a higher weighting to the commodities which have increased most?

Mr. YOUNG. We are using in this particular index revision the results of the Census of Manufactures of 1954 which we were not able to use earlier. It does give a somewhat different weighting.

The CHAIRMAN. This is a technical problem. It has been some years since I have worked on index numbers.

You change your index numbers either by getting more accurate data on series already included or by getting new commodities which previously had not been covered or by changing the weighting system as to the relative importance given to the ingredient items.

What I am trying to find out is, if the Congressman will permit this, whether this increase is due in part, and, if so, what part, to the change in the weighting system?

Mr. YOUNG. It would be due in a small part to the change in the weighting system. On the old weighting system, a revised index would have come out even higher than Chairman Martin stated.

The CHAIRMAN. Will you get a qualitative estimate as to the three types of change?

Mr. YOUNG. We will. We will provide a complete description of our procedures in, I think, either the September or October issue of the Federal Reserve Bulletin.

The CHAIRMAN. Of course, the changes in the total index affected by changes in the weighting system are much more conjectural in nature than changes resulting from the first two factors.

Mr. YOUNG. Senator, in connection with this particular revision I would like to say here that we had an unusual opportunity to test alternative weighting systems in this instance because we had this entirely on an electronic computer and it was possible to check all conceivable weighting systems that were applicable.

The CHAIRMAN. We shall await with interest your results.

Mr. YOUNG. And I should like to add that we consulted with a group of outside experts in making our final choice on the weighting system.

The CHAIRMAN. I apologize, Congressman, for taking your time. It will not be charged to you.

Representative COFFIN. With this new revision, these figures are not quite comparable to figures for prior decades because you added electrical energy for one item; is that correct?

Mr. YOUNG. When we revise the index it is true that for a period of time there will be a gap between what we can show for this most recent decade and what we have for earlier decades.

But as soon as what we are able to carry the undertaking backward we will get that accomplished, too. It is a matter of considerable effort; it will take quite a bit of time.

Representative COFFIN. I yield back my time, Mr. Chairman.

The CHAIRMAN. I think you have more time. I took out some time.

Representative COFFIN. It is all right. I have exhausted myself.

The CHAIRMAN. Mr. Martin, I regret I was not here this morning, but I have read some of your letters and statements.

Do I understand that it is your contention that if the Federal Reserve carries out open market operations that this will increase member bank reserves?

Mr. MARTIN. You mean if we purchase securities? Yes, indeed.

The CHAIRMAN. Yes, I thought it was obvious. And that this will lead to member banks loaning more money, more credit; except possibly in a period of depression? That is to say if member bank reserves increase, they will take advantage of their increased lending capacity and lend more credit to borrowers.

Mr. MARTIN. When there is a demand for credit; yes, sir.

The CHAIRMAN. With existing reserve requirements at the ratio of 6 or $6\frac{2}{3}$ times the increase in their reserves; is that not right?

Mr. MARTIN. That is correct.

The CHAIRMAN. Do I understand you to say that when the Federal Reserve carries out open market operations such as is advocated in the Reuss resolution, that this is inflationary?

Mr. MARTIN. Under present conditions, Senator, in the context in which we are operating, I felt—I know that Mr. Reuss is perfectly sincere in believing—

The CHAIRMAN. We are all sincere. It is a question of accuracy; that is all. We are just as sincere as Mr. Reuss. I hope I am just as sincere as you are. So let us sweep that off the boards. The question is whether the Reuss resolution is inflationary. I think you said it is.

Mr. MARTIN. In my judgment it is. In my judgment it will not help the Treasury and it is inflationary.

The CHAIRMAN. It is inflationary?

Mr. MARTIN. In the present context.

The CHAIRMAN. I seem to be interrupting, but I always think you have finished your sentence.

I note that in a letter to Congressman Simpson you termed the Reuss resolution as one that would involve printing press money.

Mr. MARTIN. That is not quite correct. I said that stripped of all its technicalities, whether it was permissive or mandatory it would make many thoughtful people, both in this country and abroad, think that this country did not have the will to manage its affairs without resorting to the printing press.

The CHAIRMAN. Then I take it that what you are saying is that since open market operations increase member bank reserves and permit member banks to lend more credit, which this will do, that this is inflationary.

Now, may I ask why is it any more inflationary than lowering the percentage of reserves which the member banks must maintain?

In the first case you increase the reserves of the member banks so that with the same percentage reserves they can loan more money.

In the other case you lower the percentages so that with the same reserves, in absolute terms, they can lend more credit.

In each case they, not the Government, lend more credit.

Now, why is it inflationary to increase the lending capacity of banks through open market operations, but not inflationary to increase the lending capacity of banks by lowering reserve ratios?

Now, this astonished me, Mr. Martin, coming from so able a man as you, who is surrounded by such eminent authorities on money, credit, and interest rates.

Mr. MARTIN. Senator, I can only answer that by saying that both will have the same end result.

The CHAIRMAN. I do not think the reporter caught that, Mr. Martin.

Mr. MARTIN. I said both will have the same end result, Senator.

The CHAIRMAN. It will increase lending by member banks?

Mr. MARTIN. In terms of reserves.

Now, under present conditions our problem is not increasing the reserves any more than a reasonable amount, so far as the flow of money is concerned, to sustain and improve the business situation. Anything beyond that, any use of the credit mechanism to create a lack of savings by bank financed operations, will be inflationary.

Now, in the context in which we are operating I have heard nobody advocating that our policy is too easy. They are all alleging that our policy is too tight.

The CHAIRMAN. Now, you are addressing yourself, if I may say so, to the quantity of bank credit to be issued rather than to the method by which the increase is to take place.

Assume, and I think you have said this yourself, assume the bank credit should expand at the rate of 3 percent a year; what difference does it make so far as the effect on the prices are concerned whether this is caused by open market operations, increasing the absolute quantity of member bank reserves, or by lowering reserve ratios, permitting the banks to credit more credit on the same absolute terms of reserves?

In each case you can get your 3-percent increase. I do not see that one is more inflationary than the other.

I am at a loss to understand how you would denounce open market operations as a means of expanding bank credit and at the same time reserve your accolade for the lowering of reserve requirements.

Mr. MARTIN. I do not denounce that means, Senator.

The CHAIRMAN. I thought you were. You called that printing press money.

Mr. MARTIN. No.

Representative CURTIS. Let us be fair as to what the gentleman said. Let him say it and not you say it.

The CHAIRMAN. My memory may be faulty, but I think in your letter to Congressman Simpson—

Representative CURTIS. Read the whole thing.

The CHAIRMAN (reading):

* * * cause many thoughtful people both at home and abroad to question the will of our Government to manage its financial affairs without recourse to the printing press.

Are you one of the thoughtful people who think that the use of open market operations would lead to the adoption of printing press money, the issuance of printing press money, or are these thoughtful people other than yourself?

Mr. MARTIN. Let me put it this way: the atmosphere in which we are operating is such that we are not in any context of producing easier money, and let me address myself to that 3-percent figure.

Perhaps it has never been wise to use that, because you are one of the foremost exponents of velocity as well as quantity in making up the measurement of the money supply.

I merely am trying to point out that so far as the reserves which we are putting into the market today, they must not be put in the context of increasing reserves beyond what is essential to a steady flow of money in the stream.

The CHAIRMAN. There is a rollcall going on. I have to leave. In conclusion I will merely say this:

I do not think there is the slightest bit of difference between these two methods so far as increasing the lending capacity of the banks is concerned. The question is how much you want to increase.

That is another point, and as one who believes in the quantity theory of money I do not want to see it rapidly outrun the index of the real national product, but there is this vital difference, however:

When you lower the reserve ratios the banks are able to create this credit without any cost to themselves and without any income to the Government.

But when you use open market operations the Government gets approximately one-sixth of the amount of credit thus credited and makes added earnings. It has no disadvantage, but it makes for added earnings to the Government.

Now I have tables here, some compiled by my staff, some compiled by the staff of the committee. I will submit for the record simply the one which we compiled which shows that if instead of the policy of lowering reserve ratios, which the Board under your leadership has followed since 1953, that expansion of credit had been created by open market operations, the net increase of revenue to the Government, i.e., 90 percent of the net profits to the Federal Reserve, in this period would have amounted to \$442,200,000 at the bond rate.

(The material referred to follows:)

Member bank earning assets—Potential expansion arising from reductions in reserve requirements, July 1, 1953, to June 30, 1959

Date	Reserve requirements as percent of deposits in—				Reduction in requirements in—					Contemporary average interest rate		Interest per annum on open market purchase of amount equivalent to Reserve reduction at—		Estimated added payment U.S. Treasury assuming equivalent open market purchase and transfer to Treasury of 90 percent of net in lieu of franchise tax			
	Central Reserve cities	Reserve cities	Country	Time deposits	Central Reserve cities	Reserve cities	Country	Time deposits	Total	Bills	Long-term bonds	Bill rate	Bond rate	Per annum at—		Cumulative to June 30, 1959, at—	
														Bill rate	Bond rate	Bill rate	Bond rate
	Percent	Percent	Percent	Percent	Millions	Millions	Millions	Millions	Millions	Percent	Percent	Millions	Millions	Millions	Millions	Millions	Millions
In effect prior to July 1953.....	24	20	14	6													
1953, July 1, 9 ¹	22	19	13		\$500	\$345	\$311		\$1,156	2.10	3.25	\$24.3	\$37.6	\$21.9	\$33.8	\$131.4	\$202.8
1954																	
June 16, 24 ¹	21			5	520	350	310	\$375	1,555	.65	2.70	10.1	42.0	9.1	37.8	45.5	189.0
July 29, Aug. 1 ¹	20	18	12														
1958																	
Feb. 27, Mar. 1 ¹	19½	17½	11½		125	195	180		500	1.35	3.25	6.8	16.3	6.1	14.7	8.2	19.6
Mar. 30, Apr. 1 ¹	19	17	11		125	190	175		490	1.13	3.12						
Apr. 17.....	18½				130	190			450	1.13	3.12	10.6	29.3	9.5	26.4	11.1	30.8
Apr. 24.....	18	16½			130					450	1.13							3.12
Total.....					1,530	1,270	976	375	4,151			51.8	125.2	46.6	112.7	196.2	442.2

¹ First-of-month or midmonth dates are changes at country banks, and other dates (usually Thursday), are the central Reserve or Reserve city banks.

Source: Based upon data from Federal Reserve bulletins and announcements.

The CHAIRMAN. That would have enabled the Government to have bought bonds during that time, reduced its borrowings and, therefore, improved the financial position.

There are other tables which we have which would indicate that if we were to change our policy in the future, that then after the 10th year we would be saving around \$85 million a year and that this would distinctly ease our financial condition and help us very much.

Now \$85 million to the Chairman of the Federal Reserve Board may not be very much, but to the Senator from Illinois it is a great deal.

Now having shot this question at you, I will go out the door.

Representative PATMAN. Mr. Curtis, are you next?

Representative CURTIS. Yes; I am. I do not know how we will handle this last testimony of the Senator from Illinois as a witness. I would have loved to interrogate him.

I think it is unfortunate the Senator did not read the full statement, the full paragraph. While he did read accurately, the part he just read was one incomplete sentence.

As I understand, one of the problems which you saw in the Reuss amendment was that having already proceeded on the theory, whenever possible, of due regard to maintaining the stability of the dollar, and without reference to any other method of maintaining reserve ratios and in context with the criticism, and political criticism I might state, of the Federal Reserve Board, this amendment could easily create this kind of thinking among people.

Am I right?

Mr. MARTIN. You are absolutely correct.

Representative CURTIS. I want to bring this thing in context. I do regret that this committee should be going along this line. There is a lot of value which can be obtained from an intelligent discussion of this issue. It is a serious one and a very important one to be discussed.

But it started out politically, I regret to say, on the floor of the House.

The problem was before the Senate, too, several months ago. It has been hammered at every day to create the impression that the high interest rate is the result of this administration and the result of the Federal Reserve, with relation to the Federal Reserve to create the impression it is not an independent agency and that it is all part of one administrative policy, when, as a matter of fact, there are two separate groups of men who have made this decision; one group, the administration, and the second group, yourself and your associates on the Federal Reserve Board.

It is entirely different impression than trying to create the idea that it is one policy rather than two groups.

In the light of the way this committee is going, I would hate to suggest it, but I think maybe we have exhausted the meat that can be gotten out of it and we are just going to get further and further into a political discussion rather than economic.

I think we should adjourn.

Representative PATMAN. Senator Douglas will be back. He had to answer a rollcall.

Representative CURTIS. I appreciate that.

It is 5 minutes of 4. In the light of the manner in which he was interrogating the witness, I am going to have to insist that a quorum is not present because I will not leave here and leave the witness to Senator Douglas.

Representative PATMAN. What if we recess for 15 minutes? How will that do?

Representative CURTIS. I think I will make a motion that the quorum is not present.

Representative PATMAN. I wish you would not do that in consideration of Senator Douglas.

Representative CURTIS. I must come to the conclusion that he would extend that kind of thing. I cannot be here and I do not know who on the minority side can.

Representative PATMAN. In 15 minutes you would have time to come back.

Representative CURTIS. I am afraid I would not regret it.

Representative PATMAN. We will just have to sit here and try to get a quorum.

Representative CURTIS. All right.

I am going to move that a quorum is not present.

Representative PATMAN. All in favor of adjourning say "Aye".

All opposed, "No".

The motion is lost.

Representative CURTIS. There is no quorum present.

Representative PATMAN. With the understanding that if the chairman wants Mr. Martin back, we will adjourn subject to the call of the Chair. We will meet tomorrow in the Supreme Court Chamber at 10 o'clock.

(Thereupon, at 4 p.m., the committee recessed, to reconvene at 10 p.m., Tuesday, July 28, 1959.)

EMPLOYMENT, GROWTH, AND PRICE LEVELS

TUESDAY, JULY 28, 1959

CONGRESS OF THE UNITED STATES,
JOINT ECONOMIC COMMITTEE,
Washington, D.C.

The committee met at 10 a.m., pursuant to recess, in room P-63, the Capitol, Hon. Paul H. Douglas (chairman) presiding.

Present: Senators Douglas, Bush, and Javits; Representatives Patman and Coffin.

The CHAIRMAN. This morning the committee will hear from representatives of the life insurance industry. I understand that Mr. Conklin will present the formal paper for the industry. He is accompanied by Mr. Badger, of the New England Mutual Life Insurance Co.; Mr. Patrick, of the Bankers Life of Des Moines—I recognize a middle westerner; Mr. Paynter, of New York Life; and Mr. O'Leary, director of economic research for the Life Insurance Association of America.

Gentlemen, we are very glad indeed to welcome you. Will you proceed in your own way.

STATEMENT OF GEORGE T. CONKLIN, JR., VICE PRESIDENT (FINANCE), THE GUARDIAN LIFE INSURANCE CO. OF AMERICA, NEW YORK; ACCOMPANIED BY SHERWIN C. BADGER, FINANCIAL VICE PRESIDENT, NEW ENGLAND MUTUAL LIFE INSURANCE CO., BOSTON; ROBERT B. PATRICK, VICE PRESIDENT, BANKERS LIFE CO. OF DES MOINES; RICHARD K. PAYNTER, JR., EXECUTIVE VICE PRESIDENT, NEW YORK LIFE INSURANCE CO.; JAMES J. O'LEARY, DIRECTOR OF ECONOMIC RESEARCH, LIFE INSURANCE ASSOCIATION OF AMERICA, NEW YORK

Mr. CONKLIN. Thank you, Mr. Chairman and members of the committee.

The CHAIRMAN. I notice you have a very formidable statement of some 50 pages. I wonder if you would be willing to summarize that and in perhaps 20 minutes, but with the understanding that the full statement will be printed in the record at this point.

Mr. CONKLIN. Yes, Senator, that was our plan.

(The statement referred to follows:)

TESTIMONY OF GEORGE T. CONKLIN, JR., VICE PRESIDENT (FINANCE), THE GUARDIAN LIFE INSURANCE CO. OF AMERICA, NEW YORK CITY, JULY 23, 1959

(Accompanied by Sherwin C. Badger, financial vice president, New England Mutual Life Insurance Co., Boston; James J. O'Leary, director of economic research, Life Insurance Association of America, New York City; Robert B. Patrick, vice president, Bankers Life Co., Des Moines; and Richard K. Paynter, Jr., chairman of the finance committee and executive vice president, New York Life Insurance Co., New York City)

I am George T. Conklin, Jr., vice president (finance), the Guardian Life Insurance Co. of America, New York City. Accompanying me are Sherwin C. Badger, financial vice president, New England Mutual Life Insurance Co., Boston; James J. O'Leary, director of economic research, Life Insurance Association of America, New York City; Robert B. Patrick, vice president, Bankers Life Co., Des Moines; and Richard K. Paynter, chairman of the finance committee and executive vice president, New York Life Insurance Co., New York City. We are glad to have the opportunity to take part in these important hearings on the Government's management of its monetary, fiscal, and debt operations. We have prepared a detailed statement which I would like to submit to be a part of the record. With your permission, I shall proceed by reading a summary of the statement, and then my associates will join me in discussing any questions the committee may want to raise.

It is our understanding that the general objective of the hearings is to explore the effects of monetary, fiscal, and Federal debt management policies upon employment, economic growth, and price levels. Senator Douglas' letter inviting us to testify further indicated that the committee "hoped to elicit suggestions of ways in which the Government's debt management operation and the Federal Reserve System's monetary operations could be improved and make a contribution to employment, economic growth, and stable price levels." It was also suggested that the committee would be interested in how the policies of ease or restraint by the monetary authorities affect the portfolio policies and other operations of savings institutions, particularly life insurance companies.

It is readily apparent that the scope of the committee's investigation is very broad and comprehensive. In order to hold this statement within reasonable limits, the focus has been placed on questions of Federal financing and management of the Federal debt. It is within this focus that we have also considered monetary and fiscal policy questions. The prepared statement is by necessity somewhat selective. It is our hope that the committee's questions will bring out issues not covered adequately in the statement.

THE OBJECTIVES OF ECONOMIC POLICY

Before entering into a discussion of Federal financing and debt management, it would be helpful to consider first the objectives of Government economic policy. In announcing these hearings, Senator Douglas stated:

"I believe that there is general agreement on two propositions: (1) that we should aim, as a nation, at the simultaneous achievement of maximum employment, an adequate rate of growth, and a stable level of prices; and (2) that the Government's most potent general tools to help bring about the simultaneous achievement of these three objectives are the practices it follows in the management of its monetary, fiscal, and debt operations."

Senator Douglas' statement suggests that these objectives are mutually compatible and are on an equal plane in importance. That is certainly our conviction. There are, however, a number of influential economists who argue that these objectives are not mutually compatible. Specifically, the basic question which they raise is whether we can, as a country, maintain full employment and vigorous economic growth without inevitably experiencing a further upward push of the cost of living. The argument is frequently made that the primary economic goals of this country under conditions of "cold war" must be full employment and vigorous growth, and that pursuit of these objectives will necessarily involve a further rise of the general price level. It is held that under full employment conditions the strong collective-bargaining strength of powerful organized labor groups will inexorably produce the wage-cost push as wages are driven up faster than labor productivity increases, with the result a rising general price level.

The argument continues that the general price rise could be prevented if the monetary and fiscal authorities of the country would act determinedly to restrain spending by consumers, business, and the Government. This they could do by Federal Reserve restriction of the quantity of money and by Federal budget surpluses. That is, the argument holds, the monetary and fiscal authorities have it within their power to prevent or curb a general price rise, but they can do so only by precipitating a sufficiently high degree of unemployment of labor to take the steam out of the wage-cost push. Such a degree of unemployment, it is further contended by these economists, sometimes termed "creeping inflationists," seriously conflicts with the basic objective of vigorous economic growth.

So, it is contended, we must as a nation choose between full employment and maximum growth, on the one hand, accompanied by creeping inflation, or on the other hand, general price stability but at the same time excessive unemployment and less than maximum economic growth. The choice we make, it is held, must be full employment and vigorous growth, even if it does mean a chronic decline in the value of the dollar. After all, the argument runs, inflation is not so terribly bad—most Americans really like it. Through various "escalators" we have learned more and more to adjust to a decline in the value of the dollar. Moreover, it is argued, there is no reason to believe that creeping inflation will have to break into a gallop—our great national output assures that inflation will remain at a creeping pace. Thus, the argument is that general price stability is incompatible with full employment and vigorous economic growth, and that we should recognize that a gradual rise in the general price level is an inevitable accompaniment of growth.

I have outlined the general argument of the "creeping inflationists" in order to contrast our own views. We believe that full employment, sustainable economic growth, and general price stability are vitally interdependent in the longer run, and that they must be pursued as a whole if we are to preserve our free economic society. This is because a national policy of inflation—even creeping inflation—would have destructive consequences for economic growth and economic and political democracy. Many of these consequences are already much too apparent as the result of the inflation we have already experienced since the end of the war. What are these consequences?

First, a continued decline in the value of the dollar is bound to injure and eventually destroy the will of the American people to save voluntarily and thereby to finance economic growth. Under our economic system the growth process springs from the willingness of the people to save some of their income and the investment of these savings in factories, mines, business concerns, homes, public works, and other capital goods. Saving is also the basic source of working capital, so important for the growth of business and industry. Who would have the desire to save under conditions in which the general price level is expected to move upward as a way of life? Who would find it attractive to invest in fixed-income obligations such as corporate bonds or mortgages under such conditions? If inflation should become generally anticipated as being inevitable, people would be driven to spending a higher proportion of their current income before it deteriorated in value. Moreover, under the expectation of inflation—creeping or otherwise—people would have the incentive not only to stop saving but also to incur debt more freely in order to accelerate their spending, for inflation robs creditors to the advantage of debtors.

If continuing inflation should become a way of life, everyone would redouble his efforts to hedge and protect against it. Escalation clauses in labor contracts designed to keep wages in stride with the increasing cost of living would spread throughout the economy. Through other measures such as increased common stock and real estate purchases, variable annuities, purchasing power bonds, and in countless other ways the American people and business would seek to ride along with rising prices. Regardless of how much escalation did occur, some elements of our society would be unprotected and would suffer because their incomes would be comparatively fixed. However, to whatever extent a stimulating effect of a rising general price level comes from the fact that some elements of society are able to benefit at the expense of others, the stimulus will be weakened as inflation becomes a way of life and means are found by many to ride along with it. Under these circumstances, it is highly likely that bigger doses of inflation would be resorted to in order to produce a stimulating effect. This is one of the important reasons why "creeping inflation" is bound to break out into "galloping inflation" as the public becomes more and more impressed by the need to guard against a continuing rise of the general price level. The history of almost every

inflation the world has experienced is that it started out as a modest creeping inflation but, as it proceeded, it sooner or later moved at an accelerating pace into galloping inflation. There is no reason that we can see why creeping inflation would not follow the same course in the United States.

A second important consequence of a continuing rise in the general price level lies in the difficulties encountered in Federal financing. As the general public's expectation of inflation grows, investors are bound to become less and less willing to purchase Government bonds because of the fixed-income nature of such securities. The difficulties become especially great when market interest rates rise above the statutory rate on long-term Government bonds, now fixed at 4¼ percent. Under these circumstances investors shift to the purchase of bonds or mortgages bearing higher interest rates—or they shift even more into equity investments of all types. Thus, the Government is compelled to rely upon short-term financing, much of which finds its way into the commercial banks, which create new money in purchasing it. The short-term Government securities which do not lodge in the banks become highly liquid assets in the hands of corporations and thus render the task of the monetary authorities more difficult in influencing the volume of spending in the economy. With corporate liquidity high, it takes more time for a restrictive Federal Reserve credit policy to have a restraining effect. Moreover, the frequent Treasury trips to the market to refinance short-term debt seriously hamper wise and effective control of the money supply by the Federal Reserve authorities. In addition, a persistent rise of the general price level makes the sale of U.S. savings bonds more difficult and tends to accentuate the redemptions of outstanding bonds. This is a highly important problem because there are over \$38 billion of E bonds outstanding at the present time, payable on demand by the U.S. Treasury.

Continued Federal deficits do much to promote inflation and the expectation of more inflation. There is little wonder, then, why most thoughtful students of fiscal policy think it is urgent that the Federal budget be brought under control.

A third consequence of inflation is that it breeds a multiplicity of Government controls and ultimately places serious curbs on our free market economy. For example, inflation is likely to lead to more and more direct controls over the free capital market. As noted earlier, rising interest rates are an inevitable market phenomenon under inflationary conditions because of the heavy demands for capital funds relative to supply. Congressional reactions we have already experienced indicate that a further interest rate rise would soon be met by legislative efforts to hold down the rise of rates through direct Government lending and Government purchases of mortgages and State and local bonds. Since interest rates are the prices of borrowed funds, if the free movement of interest rates is restricted by Government, the result would not only be policies which would accentuate inflation but also the spread of a network of direct Government controls over where capital funds can be employed and on what terms.

Moreover, continuing inflationary measures would ultimately lead to the spread of direct Government controls over wholesale and retail prices. As we learned so well during World War II, these controls are not effective in stopping inflation because of the breakout of "black market" transactions. This is why, as we go the route of direct Government controls, they are bound to multiply and become more pervasive. Under these circumstances could the freedom of labor to bargain collectively remain intact? It seems inevitable that wages would be brought under control, and this would ultimately restrict the freedom of the worker to select his own job.

America must remain strong to protect herself and her allies against the threat of Soviet tyranny. This means that we must maintain high employment of our resources and vigorous economic growth. But, we must find the way to do this within the limits of general price stability, for continued inflation would undermine the willingness of our people to save, which is the source of growth. It would also destroy the very system of political and economic democracy which we are so anxious to preserve.

FEDERAL FINANCING AND DEBT MANAGEMENT POLICIES

Developments in the past year in the Government securities market, and in the national economy as a whole, indicate the desirability of a reexamination of the U.S. Treasury's financing and debt management policies. The heavy cash financing and refunding operations which must be undertaken in the months ahead made such a reexamination particularly timely.

Our discussion of this subject is divided into two main sections. The first considers the Treasury's financing and debt management policies in the perspective of postwar developments in the capital market and the national economy as a whole. The second section considers a number of specific questions regarding Federal financing and debt management as follows: (1) What should be the basic considerations behind Federal debt management policy? Is the objective of lengthening the average maturity of the Federal debt so important that the Treasury should take advantage of every opportunity to sell longer term bonds even in periods of general economic recession? (2) What maturity distribution of the marketable Federal debt should the Treasury work toward? (3) What can be done to restore the market for long-term marketable Government bonds? (4) Should the Treasury undertake a program of advance refunding? (5) Are there any new or improved market techniques which the Treasury should adopt to expand or improve the market for Government bonds? (6) Are there any measures that can be taken to improve the net sales of savings bonds? (7) Should the Treasury issue a new type of "purchasing power bond" in which the amount paid to the holder at maturity is tied to the index of consumers' prices?

THE TREASURY'S FINANCING AND DEBT MANAGEMENT POLICIES IN PERSPECTIVE

The problems of Treasury financing and public debt management can only be studied profitably against the background of conditions in the capital market and the economy as a whole. Competing demands for loanable funds have a profound effect on Treasury policies, so that it is important to analyze the trends in these competing demands. Likewise, trends in the flow of long-term capital funds also must be viewed in perspective, as well as the trends in public policy in important areas such as housing, residential mortgage lending, and foreign aid and investment.

During the postwar period, with comparatively moderate interruptions, our national economy has functioned at capacity or close to capacity, and we have achieved a commendable growth in national output. Measured in current prices (i.e., without correcting for price changes), gross national product increased from \$211 billion in 1946 to \$438 billion in 1958, a rise of 108 percent. Expressed in 1958 dollars, however, GNP rose from \$312 billion in 1946 to \$438 billion in 1958, for a real increase in output of 40 percent. Associated with this growth was a most unfortunate rise of over 48 percent in prices. The inflation which has occurred is a highly important force affecting Treasury financing today.

Analysis of the capital markets in the period 1946-58 confirms the above figures. During most years in this period the demand for capital funds from both private and public users has been so great as to outrun the supply of savings. As a natural outgrowth of pent-up desires during the war, as well as other forces such as population growth and technological changes, the postwar demand for capital funds to expand and modernize industry, to build homes, to construct schools, highways, and other public works, and for other capital improvements, has been so enormous as to press sorely against the relatively limited supply of savings. In addition to the purely domestic demand for long-term funds, there has been a heavy draft on the capital market to finance both public and private commitments abroad. Repeated Federal deficits have contributed much to the demand for funds.

The excess of demand for capital funds over the supply of savings has persisted despite the fact that during 1947-58 the total of capital funds available from savings sources rose from \$16.9 to \$28.7 billion, as shown in table 1. This increase in the dollar amount of savings was to a limited extent the product of the growth of national income in real terms, but it was also largely the product of the inflated price level and the inflated money incomes of the period. Inflation does raise the level of money incomes and thus produces a greater aggregate of money savings, but not real savings. However, as noted earlier, continued inflation is bound to weaken the urge to save and thus the rate of saving by our people. Moreover, as figures presented subsequently demonstrate, inflation raises the demand for capital funds much more than it does the total dollar amount of saving.

As the demand for capital funds exceeded the supply of savings in many of the postwar years, the gap was filled by an increase in the supply of money resulting from an expansion of commercial bank credit. The pressure of this expanded money supply in the capital goods fields, with its subsequent ramifications throughout the rest of the economy, contributed to inflationary pressures

and provided a climate favorable to the wage-price spiral. Excess demand for goods using this money and the wage-price push teamed to ratchet up prices.

The demand for capital funds has been great in the field of residential construction. Chart 1 and table 2 show the large and rising use of capital funds in residential mortgage financing during 1947-58, as well as the use of funds in farm and commercial mortgage financing. A major portion of capital funds throughout the postwar has been employed in residential mortgage financing. It should be noted that the data employed here measure the net increase in outstanding mortgages. There is little doubt that the large output of housing in the postwar period, and the heavy demand it has placed upon the supply of capital funds, has been to a large extent a direct outgrowth of Government policy—namely the promotion of very low downpayment (often no downpayment), long amortization loans insured or guaranteed by the Federal Government. The availability of this type of financing has made possible an effective demand for housing by a large proportion of our families. From a social viewpoint, it is gratifying that good housing is now available to such a large percentage of our families. Further progress is needed. But, if our national economy is to grow soundly, housing and other capital improvements here and those we are paying for abroad must be fitted within the limits of our voluntary savings.

At periods in which private sources of capital funds have not been plentiful enough, at rigidly fixed interest rates, to meet congressional desires for FHA and VA mortgage financing, the supply has artificially been expanded through purchases of such mortgages by the Federal National Mortgage Association and direct Government lending. Too often this money for FNMA purchases and direct Government lending has resulted from an expansion of commercial bank deposits and the money supply. It has thus had an inflationary impact in the residential construction field and consequently in the economy as a whole. It is significant that during the period from 1946 to 1958, the Boeckh index of residential dwelling unit construction costs rose 73 percent, whereas the BLS wholesale commodity price index rose 51 percent and the index of consumer prices 48 percent. The reason why FNMA purchases have been inflationary is that FNMA debentures have usually found their way into commercial banks; also, too often the funds financing direct lending by the Veterans' Administration have been raised by the Treasury by means of security sales to the commercial banks. Usually an expansion of direct Government loans and FNMA purchases has conflicted with Federal Reserve efforts to restrain inflationary forces.

Throughout this period, as the Federal Government has become more and more active in the housing and mortgage field, individual investors and financial institutions have come to accept the Government-insured and guaranteed mortgage as a desirable and comparatively attractive outlet for their funds. This has been doubly true because Government policy has endeavored to encourage investment in these mortgages. Indeed, the readiness with which Congress has been willing to expand direct Government lending and FNMA purchases has placed pressure on investors to make mortgage loans in order to avoid having Government replace private capital in the residential mortgage field. Of particular significance for the Treasury in its financing efforts is the fact that the net yield to investors (after all costs) on FHA and VA mortgages has consistently been appreciably higher than the yield on long-term Government bonds. For example, at the present time FHA and VA mortgages at the maximum $5\frac{1}{4}$ percent rate can be readily purchased at a price of 96 or lower to produce about a 5½ percent gross yield assuming a 12-year average life of the mortgage. The net yield on such mortgages to a life insurance company after servicing and home office costs would be over 5 percent. The current yield on Government bonds with comparable maturity is about $4\frac{1}{4}$ percent. The fact is that in spite of the higher net yield on FHA and VA mortgages as compared with Government securities, the supply of funds from private investors for investment in Government-insured and guaranteed mortgages has been decreasing somewhat in recent months because of a better net rate of return after costs to be earned on corporate bonds and conventional mortgages. At frequent intervals in the past several years, the supply of Government-insured and guaranteed mortgage funds from private investors has declined sharply because the rate of return on them did not keep pace with other interest yields available to investors.

It is apparent, therefore, that FHA and VA mortgages (not to mention conventional mortgages and corporate bonds) present stiff competition to the Government bond market. This has consistently been true throughout the postwar

period. Through its program of residential mortgage insurance and guarantee the Federal Government has brought into being an investment instrument which is considered to have little more risk than a Government bond but which pays a markedly higher net rate of return. Steadily rising quoted real estate values in the inflation have fortified the belief of little risk in an FHA or VA mortgage. It is little wonder, then, that many investors have substituted FHA and VA mortgages in their portfolios for Government bonds. During the period 1946-58, for example, the net increase in life insurance company holdings of VA and FHA mortgages amounted to \$13.5 billion, or over 21 percent of the total net increase in assets during this period. Even more strikingly, the net increase of mutual savings banks' holdings of VA and FHA mortgages in the period amounted to \$13.5 billion, or 65 percent of their net increase of \$20.8 billion in total assets.

The above discussion has been in terms of the huge demand for Government insured and guaranteed mortgage loans and the competition such mortgages offer to Government bonds. The difficult competitive position of the latter is quite clear. In addition, there have been federally guaranteed ship loans and bond issues of various Federal agencies such as the Home Loan Bank System which compete with the U.S. Treasury for funds. But, it should also be kept in mind that throughout the postwar period there has been a consistently large demand for "conventional" or uninsured mortgage loans, both residential and commercial and industrial. These are included in chart 1. Generally speaking, the net yield on the conventional loans, even after allowing for somewhat greater risk of loss, is higher than the net yield on FHA and VA mortgages. Moreover, as noted below, the net yield on high-grade corporate securities directly placed with institutional investors has consistently been within the same range as the yield on conventional mortgages.

The postwar capital market has also witnessed a very large and growing demand for funds by business and industry. Chart 2 and table 3 depict the uses of capital funds in corporate financing, 1947-58. The figures again show the net increase in corporate securities outstanding each year. It should be kept in mind that the figures on corporate financing do not include funds from retained earnings. They measure just the funds obtained through the capital market. Neither did the figures on residential mortgage financing take account of equity payments in the financing of housing.

From the standpoint of the Treasury's ability to compete with heavy corporate demands upon the capital market, it should be noted that the 52-percent corporate income tax rate has reduced the effectiveness of an interest rate increase as a deterrent to corporate borrowing. Since interest cost is a deductible expense in business taxation, the effect of a rise in borrowing costs to a business concern in the higher tax brackets is cut in half. Moreover, it is also important to keep in mind that double taxation of corporate earnings has militated against financing through the sale of stock and has thus contributed to a greater proportion of bond financing. The combined effect of the above-mentioned factors and the heavy demand for capital funds by business and industry has made it difficult for the Treasury to bid successfully for long-term funds. This has been especially true in that, after a decade of very few business and industrial failures, many investors have come to regard corporate bonds practically as riskless as Government securities. The result is that the risk element in the yield "spread" between corporate bonds and Government bonds has narrowed in the postwar period. Figures were given earlier to illustrate how hard it is for the Treasury, within the range of interest rates it has offered to date, to compete with yields on FHA and VA mortgages. There are no readily available data showing average yields on high-grade corporate bonds directly placed with investors or the net yield on conventional mortgages. However, because of the competitive forces which govern the flow of life insurance funds into investment, it is certain that the net yield on direct placements and conventional mortgages at the present time exceeds the rate on FHA and VA mortgages because, as noted earlier, the flow of life company funds into these mortgages is slackening in favor of direct placements of corporate bonds and conventional mortgages. In recent years the rate on high-grade corporate bonds directly placed has consistently been greatly in excess of the rate on long-term Governments. Or put another way, the spread between the yield on long-term Governments and the yield available on high-grade direct placements has been too large to persuade investors to purchase Governments.

Chart 3 and table 4 show the combined uses of capital funds in mortgage and corporate financing in 1947-58. Chart 4 and table 5 show the net use of funds in

Federal financing and the steady rise in State and local government financing as a user of capital funds. In this latter instance, the tax-exempt feature has made it possible for State and local government borrowing to compete on very favorable terms with the U.S. Government. Indeed, the tax-exempt feature has enabled State and local securities to capture a large part of the savings of individuals. As indicated in chart 4 and table 5, the Federal Government was a net user of capital funds in the market in 7 of the 12 years, 1947-58, with the total amount borrowed equal to \$36.4 billion. This demand has been a key factor in the capital markets throughout most of the period.

In addition to the huge demands for capital funds for residential mortgage financing, corporate financing, and State and local government financing in the postwar period, and the appreciably higher return to investors in these outlets, there is one other very important force which has probably acted to place the U.S. Treasury at a disadvantage in its efforts to sell long-term bonds. That is the inflationary psychology which has developed in the minds of many Americans. This is particularly evident today, but it has been growing for some time. A manifestation of this psychology has been the rise of the stock market in the past several months. The deep roots of this inflationary psychology are demonstrated by the fact that it persisted in the face of a business recession last year. It is undoubtedly bred of despair about the inability to get Federal spending under control. Contributing also is a belief in the inevitability of the wage-price spiral due to the great bargaining strength of organized labor, as well as the strong political support for measures to maintain full employment.

The inflationary psychology is, of course, to be deplored. The purpose in discussing it here is to point out that its existence has an important effect on the capital markets, and hence on Treasury financing, especially the sale of long bonds. As noted earlier, with more and more people accepting the inevitability of inflation, investors have become increasingly hopeful that they can find a way to hedge against it through investment in equities. This is particularly true of individuals who should provide a substantial market for Government securities. The decline in the value of the dollar, and the expectation of further inflation, militates against the sale of fixed-income securities. Investors who continue to buy bonds and mortgages recognize that a higher level of interest rates is needed, not only to compensate for the use of the funds, but also to take account of the fact that the dollars paid back may well have a reduced purchasing power. Thus, as pointed out earlier, an inflation premium becomes part of the interest rate. Accordingly, it seems certain that if the inflation psychology persists, long-term interest rates are likely to shift to a higher level. The movement of interest rates since last spring probably is explainable in these terms to some extent. Thus inflation itself and the investor psychology it nurtures make more difficult the sale of long-term Treasury bonds.

In summary, during the postwar period the ability of the U.S. Treasury to sell long-term bonds has been reduced sharply and the problem of maintaining a balanced maturity distribution has become more and more difficult. This is primarily because of the huge competing demands for capital funds in the private sectors of the economy and for State and local financing which too often have exceeded the total supply of savings. These competing demands, encouraged and even stimulated by Government housing and tax policies, have outbid the U.S. Treasury in obtaining the available funds. The inflation engendered by an expansion of the supply of money to supplement savings, along with the wage-price spiral, has itself made it more difficult to sell long-term Treasury bonds.

This review of the Treasury financing and debt management in the perspective of the capital market and the national economy as a whole in the postwar period suggests that the following basic steps must be taken if the market for Government bonds is to be broadened:

- (1) The Federal Government and the Congress must together concentrate vigorously with all fiscal, monetary, and other appropriate policies to bring an end to inflation and to destroy the psychology of inflation. Sound Government financing requires that in periods of high prosperity the Federal Government should run a budgetary surplus and should retire some of the debt. This is a principle which has been too easily overlooked in the postwar period, as is shown in chart 4. Failure to implement this principle has made the Treasury financing and debt management problems much more difficult. In fact, it is hard to see how debt management problems can be solved unless Federal budgetary policy is conducted on a sound basis.

The Employment Act of 1946 should be amended to make it clear that general price level stability is a goal of equal importance with full employment and economic growth. Moreover, Government must cease temporizing with the wage-price spiral. The difficulties involved here are not to be minimized, but inflation is man made and can be brought under control by intelligent and determined action. The cooperation of private elements in the economy is, of course, essential, but leadership must come from the Government and Congress.

(2) Foremost in the fight against inflation, we need better understanding of the fact that the only source of genuine growth in our national economy is real investment and the requisite saving to finance it. As a country we have been attempting to grow faster than our national saving justifies. Too often we have resorted to the creation of money to finance the growth beyond what we have been able to finance through savings. We have learned the painful lesson that capital expenditures financed by an increase of the money supply under boom conditions are the certain way to inflation.

(3) Careful attention must be given to reforms of the Federal tax system which would encourage saving and investment. In view of the shortage of savings relative to the demand for capital funds which has characterized the post-war period, and which will continue in the foreseeable future, our tax system needs to be subject to careful study to eliminate forms of taxation which unnecessarily discourage saving. This is not an easy task, in view of the heavy revenue requirements of the Government, but the need is clear in terms of the great demands ahead for capital funds. Toward the same end, interest rate policies of the Federal Government should be reexamined to see if they are consistent with the requirement of greater saving. The level of interest rates has an important influence on the willingness of people to save.

(4) The only possible way for the Treasury to raise long-term funds on a sound basis in a free capital market is to pay the interest rate required to bid funds away from other users. The Treasury task of bidding for long-term funds will be eased to the extent that steps outlined in the foregoing three parts of this summary are carried out. If the Treasury is to be in a position to bid for long-term capital funds, it must be free to meet the going market interest rate.

Specific questions of Federal financing and debt management

Against the background of the foregoing discussion, I would now like to turn to several specific questions of Federal financing and debt management.

1. *What should be the basic considerations governing Federal debt management policy?*—Since the middle thirties a widely accepted theory of Federal debt management has been that in a period of declining general business activity the Treasury should limit its financing (either new money or refunding) to short-term securities suitable for commercial bank purchase, with the thought that this would lead to an expansion of bank deposits and thus have a stimulating effect on business. On the other hand, according to this theory the Treasury should sell long-term bonds to nonbank investors in a boom and thus draw funds away from private financing in order to exercise a restraining effect on business. This theory of debt management was linked to the related idea that Federal budgetary deficits should be incurred in a business decline and surpluses in boom periods. Thus, debt management was viewed as an important tool to be employed by Government along with fiscal and monetary policy to combat the business cycle.

Several times in recent years this issue has come to the fore as the U.S. Treasury has sought to sell long-term bonds in order to lengthen the average maturity of the debt. In June 1958, specifically, the decision of the Treasury to sell a moderate amount of a long-term bond was roundly criticized in some quarters on the grounds that such a bond would interfere with business recovery. It was argued that instead the Treasury should concentrate all of its financing in short-term securities for commercial bank purchase.

The experience of recent years has proved that this theory of debt management has usually, as a practical matter, led to very little long-term Treasury financing. There never has seemed to be a good time to sell a long-term bond. Either the sale of such a bond seemed unwise because it would hamper business recovery, or it was considered out of the question in a boom because it would hurt prosperity or require too high an interest rate for the Treasury to pay.

Our conclusions regarding the basic considerations governing Federal debt management are as follows:

(1) Debt management should not be regarded as an important tool to be employed by Government in combating the business cycle. Government efforts to counteract the cycle have much greater potentialities in the areas of monetary and fiscal policy.

(2) The objective of lengthening the average maturity of the Federal debt has proved so elusive, yet is so important, that the Treasury should take advantage of every opportunity to sell longer bonds. This means that efforts should not be relaxed to sell long bonds in periods of high business activity. It also means, as a practical matter, that the Treasury must be alert to the opportunity of selling long-term bonds even in periods of general business slack. If there is an accumulation of long-term funds available to purchase Government bonds, the Treasury should make such bonds available even though a business recession may exist. If such sales do seem to interfere with business recovery, monetary policy measures can be used to aid in correcting the situation.

(3) Treasury financing and debt management operations should be aimed primarily (as discussed more fully later) at developing a maturity distribution of the debt which will reduce to a minimum the number of trips to the market by the Treasury. A major objective should be to manage the debt in a way so as to interfere as little as possible with the freedom of the monetary authorities.

2. What maturity distribution of the marketable Federal debt should the Treasury work toward?—In view of the great practical difficulties which the Treasury has experienced in lengthening the average maturity of the debt, this might seem to be a fruitless question. We believe, however, that it is of vital importance that the Treasury work toward a better maturity distribution.

The ideal maturity distribution of the Federal debt is one which would produce a smooth, regular, and steady flow of maturing issues by means of an orderly spacing of outstanding issues. Table 6 presents a hypothetical debt distribution, based on a total marketable debt of \$180 billion, which would produce such a flow of maturing issues, and also shows the new issues required to keep this maturity distribution unchanged over time. The table was drawn up merely to illustrate certain principles; the proportions in each maturity class could be varied considerably without altering these principles.

It will be observed that in the hypothetical maturity distribution in table 6, \$57 billion would be in bonds with a maturity of 5 years and over, or nearly one-third of the total debt. The portion of the debt with a maturity of 10 years or longer totals \$37 billion, or about 20 percent of the total. Some students of Treasury financing and Federal debt management would question whether this latter percentage is high enough. Others would question the need for having a substantial portion of the debt such as 20 percent in the longer maturity ranges. They would hold that the case for extending the average maturity of the debt is not a strong one and that the Treasury would be perfectly well off to confine its financing to short-term securities and to abandon efforts to sell longer term securities. We believe that this argument is not sound and that there are highly important reasons (discussed in the following paragraph) for the Treasury to strive for a balanced maturity distribution with a substantial proportion of longer term bonds.

A well-balanced maturity distribution would have advantages for the Treasury, the capital market, the Federal Reserve, and the economy as a whole. Advantages to the Treasury are that a "bunching" of maturities in the face of possible uncertain market reception would be alleviated, and the size and frequency of refunding operations involving decisions on new terms would be reduced. In so doing, Treasury efforts to raise new cash for seasonal needs or budgetary deficits would be less subject to interference from large refunding operations with uncertain market reception and attrition. Perhaps most importantly, in view of the uncertain international political situation, it makes sense for the Treasury to have a substantial portion of its debt in a long-term form in order to leave adequate room for emergency financing. From the viewpoint of the capital market as a whole, a more even flow of Treasury maturities and greater certainty about the standard disposition of maturing issues would be advantageous, for it would mean less interference with the basic pattern of corporate, real estate mortgage, and State and municipal financing. It would also mean less uncertainty about shifts in the term structure of interest rates. From the standpoint of the Federal Reserve and the preservation of economic stability, an orderly spacing of maturities and a reduced frequency and size of refunding operations would allow far greater freedom to pursue credit poli-

cies consistently. The frequent Treasury trips to the market when so much of the Federal debt is short term greatly handicap the use of monetary control measures.

For all of these reasons, therefore, we believe that the primary objective of debt management policy should be a well-balanced maturity distribution in which longer-term issues constitute a substantial proportion.

3. *What can be done to restore the market for long-term marketable Treasury bonds?*—This is, of course, the No. 1 problem of Treasury financing. Before launching into consideration of it, it will be helpful to review the facts on trends in ownership of the long-term marketable debt. Table 7 shows the total outstanding long-term Treasury bonds, by type of investors, in the period 1945 through March 1959. Long-term bonds are defined here as those due or callable in 10 years or over. Included in the figures are the investment series B bonds of 1975-80. Although these bonds themselves are nonmarketable, they are exchangeable for marketable 1½ percent 5-year Treasury notes, and hence it seems desirable to include them. The table needs little comment. It shows that the total outstanding long-term Treasury bonds declined steadily from \$59.8 billion at the end of 1945 to \$15.2 billion at the close of 1957, with a moderate rise to \$16.8 billion at the end of 1958. It stood at \$17.4 billion at the close of March of this year. Although not shown on table 7, long-term Treasury bonds amounted to 30 percent of the total outstanding marketable Federal debt at the end of 1945. By the end of 1957 this percentage had fallen to 8.7 percent. At the end of March 1959 it was 9.4 percent. The table shows the steady and pronounced decline in holdings of long-term Government bonds by commercial banks, mutual savings banks, life insurance companies, fire, casualty and marine insurance companies, and "all other investors" through 1957. This latter category includes not only individual investors but also banks and insurance companies not reporting in the Treasury survey, trust funds, corporations, uninsured pension funds, and others. The uninsured pension fund holdings are shown separately as a "memorandum" item from 1953 on. Even the category "U.S. Government Investment Accounts and Federal Reserve Banks" has shown a tendency to decline since 1951 after Federal Reserve support of the Government bond market was abandoned. All of the groups in the table increased their holdings moderately in 1958.

Table 8 shows the holdings of long-term Treasury bonds by type of investors as a percent of the total of such bonds outstanding, from 1945 through March 1959. As noted in table 7, the total of long-term bonds outstanding declined sharply in this period, so that the percentage figures are measured on a declining base. The figures show that as the outstanding amount of long-term Federal debt has declined, the broad category "all other investors" and "U.S. Government Investment Accounts and Federal Reserve Banks" have become proportionately larger holders, whereas the commercial banks and life insurance companies have shown a declining percentage. The percentage figures for the mutual savings banks and the property insurance companies showed considerably more stability, but even here a decline has occurred in recent years.

The explanation for the steady decline in holdings of Government bonds by most investors is quite clear. As noted earlier, with the great demand for capital funds from business and industry, homeowners, and State and local governments, investors have been moved by competitive forces to place their funds where the rate of return is more attractive than in Government securities. This is illustrated by the following series of charts and tables. Chart 5 and table 9 depict the net uses of funds in selected investments of mutual savings banks, 1947-58. The negative figures on U.S. Government securities indicate, of course, net reduction in holdings. Chart 6 and table 10 show net uses of funds in selected investments by corporate uninsured pension funds, 1947-58. Chart 7 and table 11 similarly show net uses of funds in selected investments of life insurance companies, 1947-58. Little comment on these charts and tables is needed. They all indicate how major institutional investors have found that the corporate bond and residential and commercial mortgage markets have offered a better investment return than the Government bond market. It should also be noted that the fastest growing savings institution in the postwar period, the savings and loan associations, have invested almost all of their funds in residential mortgages. The net amount of funds brought into the capital markets annually by savings and loan associations increased from \$1.4 billion in 1947 to \$6.2 billion in 1958. Out of total net funds of \$40.6 billion brought to the capital markets during 1947 to 1958, inclusive, by the savings and loan associations, \$37.7 billion, or 93 percent, have gone into residential mortgages.

It would perhaps be helpful to comment particularly on the reduction in holdings of U.S. Government securities by the life insurance companies. At the end of World War II the life insurance business had nearly 46 percent of assets invested in U.S. Government securities. This was, of course, the result of a natural desire on the part of life companies to aid in the war financing, as well as the general unavailability of private investment outlets in a wartime economy. As the private economy expanded in the postwar period, it was to be expected that life companies would move to redress the balance by concentrating their investments in the areas of corporate securities and mortgages. This was all the more necessary because the rate of return on U.S. Government bonds during the war was below the rate generally assumed by the life insurance business in policy contracts. There is a high degree of competition between companies to earn the highest possible return on investments because a favorable return makes possible a lower cost of insurance to policyholders. Life companies recognize, of course, the responsibility they have to policyholders to earn the highest possible return on investments consistent with safety of the principal. Not only does this competition exist as between life companies, but more and more in recent years the rate of return earned by life companies has been a factor in their competition with other institutions competing for the Nation's savings, such as uninsured pension funds, mutual funds, mutual savings banks, and savings and loan associations.

Accordingly, it has been natural for the life companies to direct their funds into real estate mortgages, corporate securities, and other outlets where the rate of return has been consistently much higher than the rate on long-term Government bonds. For the same reason, it has been natural for life companies to dispose of Government bonds in order to respond to heavy demands for capital in the private sectors of the economy. It is interesting to note, however, that the combined life insurance company holdings of U.S. Government securities and Government-insured and guaranteed mortgages at the end of 1958 amounted to \$22.3 billion, or about 21 percent of total assets. If Government-guaranteed ship loans and U.S. Government agency bonds were added, life insurance company holdings of direct and guaranteed debt of the Federal Government would amount to about 22 percent of assets.

During the postwar period, with the amortized mortgage coming into full bloom, and with sinking funds becoming the practice in corporate financing, the life insurance companies now have an annual cash flow of roughly double their increase in assets. This means that they have a high degree of built-in liquidity which greatly reduces any need to rely on Government securities as a source of liquidity.

Against the background of the trends we have reviewed, similar as we have seen for most long-term institutional investors, what if anything can be done to restore the market for long-term marketable Government bonds? The solution to this problem is a difficult one because there have been powerful forces behind the trends of the postwar period. There are many who believe that the answer lies in new types of marketable Government securities and improved sales efforts to appeal to individual investors, to personal trust funds, and to other investors than the major savings institutions. There are also many who believe that ways can be found to increase sharply the net sales of savings bonds to individuals so that a portion of the marketable long-term debt can be shifted to the nonmarketable category. Both of these possibilities are considered later. There are others, however, who hold that in addition to broadening the market with individuals it will still be necessary to find ways to bring the major savings institutions back into the Government bond market as net purchasers, at least on a limited scale. This leads, then, to the question of what can be done to accomplish this objective.

Let us first consider this question with respect to the life insurance companies. The basic nature of the problem is about the same for mutual savings banks, uninsured pension funds, and other institutional investors. What can be done to bring the life companies back into the Government bond market as net purchasers? The heart of the answer lies in the yield offered on Government bonds versus the rate of return on other investments. The all-important step for the Treasury is to offer an interest return fully competitive with the yield on other investments. This the Treasury has not done in recent years despite much talk about "competing in the market." As pointed out earlier in this report, the interest rate on long-term Government bonds has consistently been much below the net yield on FHA and VA mortgages, an investment area in which there has been great public pressure for life companies to participate. Moreover, the rate

on Treasury bonds has been consistently much lower than the return on direct placements of high-quality corporate bonds and conventional mortgages. The spread between the yield on new issues of Government bonds and the yield on new offerings of high-grade corporate bonds directly placed, or conventional mortgages, has consistently been too great to make Government bonds attractive to life insurance companies, or most other institutional investors. The interest rate placed on new offerings of Government bonds has generally been set slightly above the yield on outstanding Government bonds of comparable maturity. It does not seem to have been adequately recognized that the market for Government bonds has been an exceedingly thin one in which the prices and yields are artificial and do not begin to reflect the market forces existing in other parts of the capital market. This is due in part to the limited supply of long-term Government bonds available. At the present time, for example, the market quotations on outstanding long-term Government bonds (due or callable in 10 years or more) indicate an average yield of about 4.10 percent. This would suggest that under present circumstances a rate of 4¼ percent on a cash offering of a long-term Government bond would be fully competitive in the market. Does this follow, however, under conditions in which FHA and VA mortgages can be purchased on a net yield basis of over 5 percent after costs, and they are now receiving a diminishing share of the flow of capital funds because investors are able to purchase top quality corporate bonds directly placed and conventional mortgages on an even more attractive net yield basis? The situation which exists today is not unique; it has been characteristic of the past several years. If the Treasury desires to broaden the market for Government bonds, it must be willing to bid realistically for funds.

Government bonds possess some favorable qualities for life company investors. For one, they are usually noncallable for nearly the entire life of the bond. In recent years in which interest rates have been subject to sharp fluctuations, life companies have come to place great emphasis on nonredeemability. They have been successful to a large extent in obtaining this in industrial bond issues, but few issues in the electric and gas utility field have provided adequate protection against early redemption. In addition, little protection is afforded against early redemption of residential mortgages. Likewise, although life companies have a high degree of liquidity, the ultimate marketability of Government bonds has some advantage. It may not be very great, however, with the Government bond market a very thin one. These qualities of nonredeemability and marketability are on the plus side regarding life company purchases of Government bonds.

As is apparent in this statement, life insurance company officers recognize the inflationary potential in the sale of Government securities to the commercial banks. They understand and appreciate the argument that enlightened self-interest suggests that life companies should purchase Government bonds to aid in the fight against inflation. Certainly the life insurance policyholders have a vital interest in a sound dollar. At the same time, the officers of life insurance companies have the responsibility to strive to earn the highest possible return on policyholders' savings consistent with safety of the principal amount. This is the basic objective which must motivate life company investments. Life insurance company funds will naturally flow into Government bonds if they are issued at competitive interest rates, and the same will be true of other institutional investors and individual investors.

It is important to bear in mind also that the normal process of life company investing in corporate bonds and mortgages involves forward commitments to make loans and takedowns of these commitments over an extended period of time. At any given time, life companies have a backlog of commitments relative to their cash flow. It would be desirable, therefore, for the Treasury to permit life companies to pay for subscriptions to Government bonds on a delayed takedown basis. This would better enable life companies to fit the purchase of Governments into their commitment picture and their cash flow expectations. Moreover, possibly some means can be worked out, using the forward commitment technique, whereby life companies enter into commitments with the Treasury to buy Government bonds on a scheduled takedown basis.

With regard to other types of savings institutions—mutual savings banks, uninsured pension funds, State and local funds, trust funds, and time deposits of commercial banks—the basic solution the Treasury problem of selling long-term bonds is the same as with life insurance companies. To restore the interest of such investors in Government bonds the Treasury must be willing to pay a

fully competitive interest rate. With some of these investors also, because of forward commitments it would be helpful for the Treasury to permit payment for bonds on a deferred basis.

What is needed fundamentally is a determined and sustained drive on the part of the administration, the Congress, and private groups to bring an end to the psychology of "creeping inflation" which has apparently become deep seated with the American people. This is a large order, but until it is done the Treasury will always find it difficult to compete with interest rates which contain a substantial inflation premium. Top-level leaders in and out of Government must come to the realization that inflation destroys the market for fixed-income investments and drives capital funds to the equity market. As noted earlier, inflation tends to shrink the rate of saving and to increase the demand for borrowed funds. Also basic to the problem of restoring the market for Government bonds with institutional investors, Congress and the administration must keep foremost in mind that as a matter of public policy the private and public demands for capital funds must be satisfied out of the voluntary savings of the American people. As these demands increase in our national economy, measures must be taken to encourage a higher rate of saving if we are to avoid inflationary pressures.

Beyond the institutional investors, are there any steps which can be taken to expand investment by individuals in long-term marketable Government bonds? In this area, even more than with the savings institutions, the need to deal a body blow to inflation psychology is clear. Otherwise the strong trend toward equities by individuals will further reduce their role in the Government securities market as real long-term investors. Assuming that something can be done to deal with inflation, the question can be raised as to whether through "hard selling" the Treasury could not market considerably more long-term bonds to individuals. Securities are sold just as anything else in this country. Should not the Treasury encourage the securities marketing machinery of the country to go out and sell Government bonds? This means the payment of commissions to brokers and dealers. Perhaps if incentives are given to salesmen the improvement in sales of Governments may be surprisingly great.

There are a number of convincing reasons why the broad mass of individual savers of the country should be a good market for Government bonds. The average individual cannot assume the risks inherent in corporate bonds because he is unable to diversify as is true of an institutional investors. Moreover, Government bonds possess a number of attributes which should appeal to the average individual saver; namely, easy and convenient methods of sale can be employed, the bonds are readily acceptable and are easily marketed, and the risk of loss if held to maturity is absent. In addition, with the average individual investor tax exemption is probably not an important factor.

Serious consideration should be given to the idea that investors who realize capital gains, but who invest the proceeds in Government securities, might be subject to a lower capital gains tax; for example, 10 or 15 percent. In order to qualify for the reduced rate, such investors might be required to hold the Government securities for some specified period such as 2 to 5 years. It is well known that investors are loathe to realize capital gains because of the tax. If the tax were reduced as suggested here, there would be a greater willingness to realize capital gains and hence there should be an appreciable increase in the flow of funds into Government securities.

4. *Should the Treasury undertake a program of advance funding?*—The advance funding last year of more than 40 percent of the Canadian Government direct and guaranteed marketable debt poses the question of whether the U.S. Treasury should not undertake similar measures.

To illustrate what is meant by "advance funding," it would be helpful to consider the investment series B, 2¾-percent bonds of 1975-80. As noted earlier, these bonds, received by investors in 1951 in exchange for Victory bonds, are themselves nonmarketable, but they are convertible into 1½-percent 5-year notes which are marketable. The total amount of investment series B bonds issued was \$15.3 billion. By the end of March of this year, nearly \$8 billion remained outstanding, so that in the intervening period \$7.3 billion had been retired. In other words, holders of \$7.3 billion of these bonds had exercised the right to convert into the 5-year 1½-percent notes.¹ Throughout this period, the sale of

¹ This figure of \$7.3 billion of retirements includes a small sum growing out of retirement on death of holders.

the 5-year notes involved a loss, but investors were able to compensate themselves for this loss over a period of time by reinvesting the funds at a higher rate of return. Thus, under conditions such as have prevailed in the capital markets in recent years, the investment series B bonds have come to be little more than 5-year notes. This issue, therefore, would seem to be a prime candidate for advance funding. What the Treasury could do would be to offer the current holders of investment series B bonds the opportunity to exchange them for a new marketable long-term issue at a yield in line with the going market rate. Holders of the investment series B bonds would undoubtedly find such an exchange attractive because they would be able to dispose of a nonmarketable bond with a low coupon, on which a substantial loss exists if the conversion is exercised and acquire a marketable bond with a yield in line with the market. The advantage to the Treasury is extension of the average maturity of the debt and stoppage of the persistent attrition on the investment series B bonds. Also, debt would be retained in the hands of nonbank investors. It would undoubtedly be argued that investors receiving the new bonds, on which presumably there would be little or no market loss, would thus be in a position to dispose of them to acquire higher yielding corporate bonds or mortgages. Whether this did take place would depend on the interest rate on the new bonds and the future course of interest rates. Regardless of this, in order for sales of the new bonds to take place there would have to be purchasers, and so far as the Treasury is concerned the bonds would remain outstanding and the longer average maturity would be retained; that is, if the new issue of long-term bonds were sold by some investors, the only market would be other long-term, nonbank investors. The new bonds could be made nonmarketable for a given period, say 5 years. Such a feature would decrease the attractiveness of the exchange and would raise questions for life companies and possibly other investors as to whether they would be legal investments unless there were some means of selling them.

The investment series B bonds are not, of course, the only Treasury issues which would be suitable for advance funding. There is a wide range of possibilities, with the $2\frac{1}{2}$ s of June and December 1964-69, and $2\frac{1}{2}$ s of March 1965-70, and $2\frac{1}{2}$ s of March 1966-71 being other good possibilities. These bonds are now coming into the commercial bank investment range and will undoubtedly find their way into bank portfolios. Then the Treasury will be faced with the very difficult task of selling new cash offering of longer term bonds to replace them if a sound debt structure is to be achieved. Through advance funding, this portion of the debt, now in the hands of long-term nonbank investors, can be kept in their hands. Moreover, a program of advance funding of the $2\frac{1}{2}$ s will open up a hole in the intermediate-term issues and thus permit the Treasury to do some extending of maturities in their maturity range.

The Treasury might find it useful to consider the desirability of combining an advance funding operation with a cash offering of a long-term bond; that is, the Treasury might offer a cash issue of a long bond and at the same time permit investors to exchange (par for par) certain other issues for the new cash offering in a fixed ratio to the cash purchases made. For example, the Treasury might decide to offer \$1 billion of 30-year bonds at a competitive interest rate. For every two bonds of the new issue purchased, investors would be given the right to exchange one Investment Series B bond (or some other ratio) on a par for par basis for the new bond. The ratio of bonds exchangeable would be adjustable, depending on how much encouragement the Treasury wanted to build up for the cash offering.

It would seem that a tie-in between a cash offering and advance funding such as outlined above could be employed successfully by the Treasury to aid in building the market for cash offerings of long bonds. The terms of the cash offering and the exchange would have to be explored carefully with the various investor groups in the light of market conditions. If the Treasury proceeded to make regular limited cash offerings, with the investor permitted to exchange holdings of certain issues of outstanding bonds for the cash offerings, investors would be encouraged to hold those securities likely to be eligible for exchange in future cash offerings. Thus, this financing method might have the collateral advantage of encouraging investors to hold outstanding bonds which otherwise might have been sold.

5. *Are there any new or improved market techniques which the Treasury should consider to expand or improve the market for Government bonds?*—The suggestion has sometimes been made that the Treasury should have a tap issue of a long-term marketable bond available for investors. Financial officers of

life companies have sometimes indicated that if a tap issue were available, they would place more funds in Government bonds than is the case when they are confronted at irregular intervals with a Government long-term issue. On careful study, it is doubtful that the availability of a tap issue would help to broaden the market for long bonds. It might improve the market with a small minority of purchasers, but actually the overall effect might well be to reduce the volume of sales of long governments. A reason for this would be that investors might come to regard the tap bond as an outlet that would always be present if nothing better could be found.

The advantages which some life insurance company investment officers have in mind in regard to a tap issue could be realized through limiting the uncertainty about allotments on subscriptions and by permitting deferred payment for Government bonds. It would be desirable to let savings institutions know in advance that they would be given a definite allotment. Every issue of a long bond by the Treasury sets in motion a guessing game as to what the allotments will be. Wrong guesses are bound to produce unnecessary disturbances subsequently in the market. There seems to be good reason, therefore, for minimizing the uncertainty about allotments. The big difficulty involved in giving out advance information on allotments is apparently that such a step would reduce the Treasury's ability to control the size of an offering. For example, let us assume that the objective of the Treasury at a particular time was to sell an issue of \$1 billion of a long-term bond. If it were certain that the market for the bond with savings institutions and other nonbank investors was about \$1 billion, then an advance announcement of 100 percent allotments to nonbank investors would be possible. The danger is that if such an announcement were made in advance, and the total nonbank subscriptions greatly exceeded expectations, the Treasury would lose control over the size of the issue. Having such control, at least within limits, is important for many reasons, the most obvious being in the example mentioned the Treasury may have need only for \$1 billion.

Ways can be found to narrow uncertainty about allotments. One step would be improved market analysis by the Treasury. Progress has been made through the Treasury advisory groups in judging the potential market for Treasury bonds. Assuming that reasonably accurate estimates can be made of the potential market for a long-term bond at any given time and at a particular rate, it should be possible for the Treasury to be specific in advance about allotments to savings institutions. This does not mean that the Treasury would always be able to announce a definite allotment, but it should be able to do so within a narrow range. Then, if savings institutions could enter their subscriptions with a high degree of certainty about the allotment, and if they knew in advance that payment could be made on a deferred basis, all of the apparent advantages of a tap issue would be achieved.

6. *What can be done to improve the net sales of savings bonds?*—During the past several years the U.S. savings bonds have lost ground as a means of saving in this country. The record in 1959 has become a source of concern. Sales of E and H bonds through May are 6 percent behind a year ago, with a worsening trend. Similarly, 1959 redemptions are 9 percent above a year ago, also with a worsening trend. On a cash basis, the net drain on the Treasury of an excess of redemptions over sales of E and H bonds in the second quarter of this year is estimated at \$300 million.

Here again the spread of inflationary psychology poses a serious threat. Unless the expectation of continuing inflation is brought under control, the Treasury will find it more and more difficult to sell savings bonds in competition with equities. Not only this, but the \$38 billion of E bonds outstanding are demand obligations for the Treasury and pose the threat of a big cash drain under inflationary conditions. Therefore, it is vital to the savings bond program that an end be made to the inflation psychology of our people.

Beyond this, it goes without saying that the interest rate on savings bonds must be kept in line with other rates if these bonds are to continue to appeal to the smaller investor. It has been argued that the sale of savings bonds is comparatively insensitive to interest rate trends, but the evidence is not convincing. Here again the basic way to induce the individual investor to purchase savings bonds is to pay an interest rate in line with market conditions. Table 12 shows the comparative yields on U.S. savings bonds, marketable bonds, and savings deposits at selected intervals since 1941. It will be noted that if held to maturity the yield per annum on series E-bonds in 1941 (when these bonds were first issued) was 2.90 percent. At this time the yield on E-bonds was most generous as compared with the average rate on marketable bonds, savings bank

deposits, and commercial bank savings deposits. It compared favorably with the rate on saving and loan shares. A similar situation existed in 1945, 1948, and 1952. Between 1952 and June 1959, however, the average yield on E- and H-bonds increased only 26 basis points, whereas the average yield on marketable long-term Government bonds increased 141 basis points and Moody's Aaa corporate bond yield index increased 150 basis points. Likewise, the average yield figures on savings banks deposits, savings and loan shares, and commercial bank savings deposits show how they have increased much more than the yield on E- and H-bonds from 1952 to 1958. These figures illustrate the need to raise the rate on E- and H-bonds to restore their early strong competitive position. The limited success achieved in recent years in the sale of E- and H-bonds is all the more remarkable in the light of the relatively less favorable yield they have as compared with other yields on savings. Given a competitive rate, savings bonds should provide a much greater source of long-term funds for the Treasury.

In addition to a competitive rate, the Treasury should also provide a system of incentives to the securities market in order to promote the sale of savings bonds. Here again, commissions should be paid to the sellers of savings bonds. Moreover, it would seem that a tax-exempt feature could be used with savings bonds that would not have a serious effect on revenues and would not cause serious difficulties of an equity nature. Such a feature could, however, have a very stimulating effect on sales of savings bonds.

7. *Should the Treasury issue bonds (either savings bonds or marketable bonds) in which the amount paid at maturity (or the amount of interest) is tied to some price index such as the index of consumers prices?*—In view of the depreciation in the value of the dollar which has occurred in the postwar period, and in view of the possibility that there may be more inflation ahead, support exists in some quarters for a purchasing power bond. It is argued that such a bond would provide investors with a hedge against inflation and should therefore help greatly to broaden the Government bond market.

We believe it would be a calamitous mistake for the Treasury to introduce a purchasing power bond. This would be tantamount to an admission of defeat in the struggle to halt inflation. If Government bonds are placed on an "escalator" along with wages, an important moral support for the fight against inflation will be lost. All branches of the Government must redouble their efforts to fight inflation and not to temporize with it. A purchasing power bond would be temporizing. Moreover, a purchasing power bond would undoubtedly enhance the expectation of inflation and could thus seriously aggravate the problem.

FEDERAL RESERVE OPEN MARKET OPERATIONS AND TREASURY FINANCING

The decline which has occurred in the prices of Government bonds during the past year has revived the argument that the Federal Reserve, through open market purchases, should support the prices of Government securities. There are some who contend that the Federal Reserve should return to the practice of "pegging" the prices of Government securities as it did during and after World War II until the Treasury-Federal Reserve "accord" in March, 1951. There are others who recognize that a pegging operation would not be in the public interest, but at the same time they contend that from time to time the Federal Reserve should purchase long-term Government bonds in order to lend stability to long-term interest rates, and at the same time sell shorter-term Government securities if such sales are required to prevent an expansion of commercial bank credit. We would like to set forth our views briefly on these two questions.

Should the Federal Reserve resume the pegging of prices of Government bonds?—After the disastrous experience under the pegging operation prior to March 1951, it is difficult to understand support for such a proposal. We certainly oppose a return to pegging of Government bond prices because it would put our country on the road to ruinous runaway inflation. The reason is clear and well understood. As the Federal Reserve purchases Government securities, it adds to the reserves of the commercial banking system and thus permits a multiple expansion of commercial bank demand deposits in the ratio of six times the reserves supplied. Thus, a pegging operation converts the Federal Reserve into an "engine of inflation" because it forces the monetary authorities to contribute to an uncontrolled expansion of the principal source of our money supply—demand deposits. It amounts to the same thing as running the printing presses to provide more and more paper money.

Under the general economic conditions existing today there could be only one result—a sharp runup of the general price level which would undoubtedly accelerate if the pegging operation were continued. As prices moved upward, and inflation psychology on the part of the public grew, there would be a number of effects which would make it more and more difficult to peg the prices of Government securities, and which would require a larger and larger volume of support purchases of Government bonds and thus greater and greater expansion of the money supply. One of these effects would be a decline in the willingness of our people to save as the dollar depreciated in value. Not only would saving dry up, but in particular, investors would be less and less willing to purchase fixed-income obligations such as bonds and mortgages. Instead, funds would move even more strongly into the common stock market and into direct ownership of real estate, and similar investments which seem to provide a hedge against inflation. There would, indeed, be a flight from the dollar into physical goods of all kinds in order to escape the effects of the declining value of money. Under these circumstances, interest rates on loans and investments other than Government bonds would be bound to rise sharply as the supply of loanable funds declined and the demand increased, for in an inflation there are positive incentives to go into debt. Moreover, as inflation psychology grew, the inflation premium in interest rates on loans and investments other than Government bonds would rise. As this situation developed, the holders of Government securities would find it more and more advantageous to sell these securities at the pegged prices because such prices would be artificially high. Thus, in order to peg the prices of Government bonds the Federal Reserve would be required to purchase a larger and larger amount of these bonds, thus heaping more and more fuel on the fires of inflation.

This is not a pretty picture, but it is inevitable if the Federal Reserve is required to return to a policy of pegging the prices of Government bonds. Actually, there is serious question today whether the Federal Reserve could peg the prices of Government securities without quickly being forced to buy an enormous amount of bonds. A great deal of change has taken place in public attitudes since the early postwar period in which the pegging operation occurred. Most important, we have experienced a good deal of inflation and the general public has unfortunately come to expect that it will continue. For this reason alone, a return to pegging of Government bonds would be a signal that the expectation of inflation was a certainty, and all of the developments outlined above would be bound to occur. So, there is really a serious question today as to whether the Federal Reserve could peg the prices of Government bonds. Certainly if it did so, the inflationary consequences would not only affect our domestic economy but they would greatly aggravate our balance of payments problems with other countries and would lead to a flight from the dollar by foreigners.

Should the Federal Reserve lend support to the prices of long-term Government bonds by buying long-term bonds and selling short-term securities?—Many who recognize the disastrous consequences of a pegging operation nonetheless argue that the Federal Reserve should conduct its open-market operations throughout the entire range of Government securities—long term as well as short. Thus, it is argued, in recent months, as the prices of long-term Government bonds declined, the Federal Reserve could have purchased the longer term issues to aid in stabilizing this sector of the market and long-term interest rates generally. It is further argued that, to the extent needed to prevent an unwanted expansion of commercial bank reserves, the Federal Reserve could have sold an offsetting amount of short-term Government securities.

To the extent that open-market purchases of long-term Government securities were matched by sales of short-term Governments, there would, of course, be no expansion of commercial bank reserves from this operation and thus no increase of the money supply. For this reason—the fact that the money supply had not changed—the Federal Reserve would not have affected the total supply of credit and presumably would not have had any influence on the general level of interest rates. So far as interest rates are concerned, the principal effect of open market purchases of longer term Government securities and matching sales of short-term securities would be to alter the interest rate structure on Government securities. That is, the purchases of long bonds would tend to make the yields on such bonds lower than they might otherwise have been, and the sales of short-term securities would increase the supply of such securities and thus make short-term Government yields higher than might otherwise have been the case.

Higher interest costs to the Treasury on short-term borrowing are very quickly translated into a higher service charge on the Federal debt because \$76 billion of Government securities mature in 1 year or less. Accordingly, taking steps which will raise short-term rates in order to hold down yields on long-term Governments is not any real solution. This is especially true when the Treasury is being obliged to concentrate so much of its financing in short-term issues and has already contributed to a sharp increase in short-term rates.

Moreover, there are other difficulties involved in an open market program of buying long-term Government securities and selling short-term securities. Such purchases would tend to hold the prices of long-term Governments at an artificially high level (or the yields artificially low) during a period of tightening conditions in the capital markets such as at present. Thus, as the yields on corporate bonds, mortgages, and State and local government securities moved upward in response to heavy demand, investors would be encouraged to dispose of long-term Government securities at the artificially high prices. The result would be that the Federal Reserve would have to increase its purchases of long bonds (as well as its sales of shorts) in order to exert the same stabilizing effect. Carried to the end, the Federal Reserve would wind up holding most of the long-term Government bonds, and short-term interest rates would be driven to a very high level, with the service charge on the Federal debt much higher in the process because of the huge volume of short-term debt.

In addition, if the Federal Reserve should begin to conduct its open-market operations throughout the entire maturity range of Government securities, it would immediately be exposed to more and more pressure to move toward pegging the prices of Governments, with all the fatal consequences this would involve.

We arrive at the conclusion that if the Federal Reserve is to retain its freedom to restrain the expansion of the money supply in a period of high and rising economic activity, which we believe to be absolutely essential, there are no manipulations of open-market operations that can escape the discipline of demand and supply forces in the capital markets. Interest rates have risen during the past year, as they always do in periods of rising business activity, basically because the market demand for capital funds has outrun the supply. The sound way to achieve lower interest rates is to encourage an increase in the supply of loanable funds or a decrease in the demand, or a combination of the two. The only way to increase the supply without further inflation is to encourage saving, and the place to start is to remove the fear of inflation itself. So far as the excessive demand for capital is concerned, the greatest force in many years has been the U.S. Government and its deficit financing. An end to deficit financing would be a potent force toward easing the capital and money markets.

SUMMARY AND CONCLUSIONS

1. The ability of the U.S. Treasury to conduct its financing and debt management operations on a wise basis is of crucial importance for the attainment of our national goals of full employment, sustainable economic growth, and general price stability. There is hardly any other matter of greater importance to the country today than that the U.S. Government be able to finance itself and manage the Federal debt in a manner consistent with these objectives. Accordingly, this statement is focused on the Treasury's financing and debt management problems, with monetary and fiscal policy questions considered within this focus.

2. Regarding the objectives of national economic policy, we believe that full employment, sustainable economic growth, and general price stability are vitally interdependent in the longer run, and that all three objectives must be pursued as a whole if we are to preserve our free economic society. This is because a national policy of inflation—even "creeping inflation"—would have destructive consequences for economic growth and economic and political democracy, as follows: (a) A continued decline in the value of the dollar is bound to injure and eventually destroy the willingness of the American people to save voluntarily and thereby to provide the only sound means of financing economic growth. Under our economic system the growth process springs from the willingness of the people to save some of their income and the investment of these savings in factories, mines, business concerns, homes, public works, and other capital goods, as well as working capital. (b) The decreasing willingness of the American people to buy Government bonds either directly or through savings institutions as the general price level rises accentuates the U.S. Treasury's financing problems and leads to the issuance of a larger and larger portion of short-term debt, thus

making inflation more difficult to control. (c) A persistent inflation is bound to breed a multiplicity of Government controls and ultimately to place serious curbs on our free market economy and thus on our economic and political freedom.

3. During the postwar period the ability of the U.S. Treasury to sell long-term bonds has been reduced sharply and the problem of maintaining a balanced maturity distribution has become more and more difficult. In no small measure this is because of the repeated Federal deficits which forced the Treasury to borrow in 7 of the 12 years, 1947-58, for a huge total of over \$36 billion. It is also because of the enormous competing demands for capital funds in the private sectors of the economy and for State and local financing which, along with Federal financing, too often have exceeded the total supply of savings. These competing private demands, encouraged and even stimulated by Government housing and tax policies, have been able to outbid the U.S. Treasury in obtaining the available funds. The inflation engendered by an expansion of the supply of money to supplement savings, along with the wage-price spiral, has itself made it more difficult to sell long-term Treasury bonds.

Our review of the Treasury financing and debt management in the perspective of the capital market and the national economy as a whole in the postwar period suggests that the following basic steps must be taken if the market for Government bonds is to be broadened:

(a) The Federal Government and the Congress must together concentrate vigorously with all fiscal, monetary, and other appropriate policies to bring an end to inflation and to destroy the psychology of inflation. Sound Government financing requires that in periods of high prosperity the Federal Government should run a budgetary surplus and should retire some of the debt. Further, the Employment Act of 1946 should be amended to make it clear that general price level stability is a goal of equal importance with full employment and economic growth.

(b) Foremost in the fight against inflation, we need better understanding of the fact that the only source of real growth in our national economy is saving and the investment of savings in capital goods. As a country we have been attempting to grow faster than our national saving justified. Too often we have resorted to the creation of money to finance the growth beyond what we have been able to finance through savings. We have learned the painful lesson that capital expenditures financed by an increase of the money supply under boom conditions are the certain way to inflation.

(c) Careful attention must be given to reforms of the Federal tax system which would encourage saving. In view of the shortage of savings relative to the demand for capital funds which has characterized the postwar period, and which will continue in the foreseeable future, our tax system needs to be subjected to careful study to eliminate forms of taxation which unnecessarily discourage saving. This is not an easy task, in view of the heavy revenue needs of the Government, but the need is clear in terms of the great demands ahead for capital funds. Toward the same end, interest rate policies of the Federal Government should be reexamined to see if they are consistent with the requirement of greater saving.

(d) The only possible way for the Treasury to raise long-term funds on a sound basis in a free capital market is to pay the interest rate required to bid funds away from other users. The Treasury task of bidding for long-term funds will be eased to the extent that steps outlined in the foregoing three parts of this summary are carried out.

4. The principal conclusions reached in this statement regarding several specific questions of Federal financing and debt management are as follows:

(a) Debt management should not be regarded as an important tool to be employed by the Government in combating the business cycle. Government efforts to counteract the cycle have much greater potentialities in the area of monetary and fiscal policy. The objective of lengthening the average maturity of the Federal debt has proved so elusive, yet is so important, that the Treasury should be alert to the opportunity of selling long-term bonds even in periods of general business slack. If there is an accumulation of long-term funds available to purchase Government bonds, the Treasury should make such bonds available even though a business recession may exist. If such sales do seem to interfere with business recovery, monetary measures can be used to aid in correcting the situation.

(b) Treasury financing and debt management operations should be aimed primarily at developing a balanced maturity distribution of the debt, with a substantial proportion of the debt in intermediate and longer term issues. Such a

maturity distribution would have important advantages for the Treasury, the capital market, the monetary authorities, and the economy as a whole. In particular, from the standpoint of the Federal Reserve and the objective of sustainable economic growth without inflation, an orderly spacing of maturities and a reduced frequency and size of refunding operations would allow far greater freedom to pursue credit policies consistently.

(c) In order to bring nonbank investors such as mutual savings banks, uninsured pension funds, and life insurance companies back into the Government bond market as net purchasers, the all-important step is for the Treasury to offer an interest return fully competitive with the yield available on other investments such as residential and commercial mortgages and directly placed corporate bonds. In addition, it is desirable that nonbank investors be permitted to pay for Government bonds on a deferred basis. This would permit such investors to fit their purchases into their forward commitment picture and their cash-flow expectations.

(d) The Treasury should give serious consideration to advance funding of some portion of the debt which has come into the shorter maturity ranges. The investment series B bonds would present a good possibility for advance funding. In addition, the Treasury should consider the desirability of combining an advance funding operation with a cash offering of a long-term bond.

(e) The Treasury should seriously consider offering incentives to the securities business to sell long-term marketable bonds. This means that the Treasury should consider paying commissions to brokers and dealers just as is done in the marketing of private securities.

(f) In order to encourage the purchase of U.S. savings bonds, the interest return on such bonds should be raised in line with the return on private investments. In addition, the Treasury should also provide a system of incentives to the securities market to promote the sale of savings bonds. A tax exemption feature should also be considered.

(g) It would be a serious mistake, to say the least, for the Treasury to introduce a "purchasing power bond" in which the amount paid at maturity (or the amount of interest) is tied to some price index such as the index of consumers' prices. This would be tantamount to admission of defeat in the struggle to halt inflation.

5. The decline which has occurred in the prices of Government bonds during the past year has revived the argument that the Federal Reserve, through open-market purchases, should support the prices of Government securities. A return to the policy of Federal Reserve pegging of the prices of Government bonds, as followed in the decade prior to March 1951, would be disastrous in that it would place our country on the road to ruinous runaway inflation. It would force the monetary authorities to foster an uncontrolled expansion of our money supply, thus promoting a sharp and accelerating rise in the cost of living, and would actually drive up interest rates on all other forms of debt except Government securities.

Some who recognize the disastrous consequences of a pegging operation suggest that, as the occasion demands, the Federal Reserve should buy longer term Government securities to afford stability to long-term rates, and at the same time sell an offsetting amount of short-term securities to prevent any net addition to commercial bank reserves and hence the money supply. Such an operation would have no effect on the general level of interest rates, but it would hold down the yields on longer term Government securities and raise the rates on short-term issues. Higher interest costs to the Treasury on short-term issues are quickly translated into a higher service charge on the Federal debt because \$76 billion of Government securities mature in 1 year or less. Moreover, Federal Reserve support of longer term Government bond prices would lead to a rapidly increasing volume of sales of such securities by private investors, and the outcome eventually would be that the Federal Reserve would wind up holding most of the long-term Government bonds, and short-term interest rates would be driven to a very high level, with the service charge on the Federal debt much higher in the process because of the huge volume of short-term debt.

If the Federal Reserve is to retain its freedom to restrain the expansion of the money supply in a period of high and rising economic activity, which we believe is absolutely essential, there are no manipulations of open market operations that can escape the discipline of demand and supply forces in the capital markets.

TABLE 1.—Capital funds available from principal savings sources, 1947-58

[Billions of dollars]

Year	Life insurance companies	Savings and loan associations	Mutual savings banks	Commercial banks ¹	Corporate pension funds
1947	3.0	1.4	0.9	1.9	0.6
1948	3.4	1.2	1.0	1.0	.7
1949	3.6	1.3	1.0	.9	.7
1950	3.7	2.1	1.0	.8	.9
1951	3.7	2.0	.8	2.3	1.3
1952	4.4	3.0	1.7	3.5	1.5
1953	4.7	3.7	1.8	3.7	1.7
1954	5.0	4.3	2.1	4.2	1.9
1955	5.3	5.6	2.1	2.2	1.9
1956	5.0	4.8	2.0	3.2	2.2
1957	4.7	4.9	1.8	6.6	2.5
1958	4.9	6.2	2.5	8.2	2.7

Year	U.S. Government ²	State and local governments	Fire and casualty companies	Individuals and others ³	Total
1947	3.4	1.1	0.8	3.7	16.9
1948	3.0	1.0	1.0	4.4	16.5
1949	2.0	1.0	1.1	3.1	14.8
1950	-.1	1.5	.8	1.9	12.5
1951	3.1	1.6	.7	1.5	17.0
1952	3.6	2.2	1.2	4.9	26.0
1953	2.4	2.5	1.3	5.1	27.0
1954	1.3	2.9	1.2	1.6	24.5
1955	2.1	2.0	.9	9.0	31.2
1956	2.3	2.4	.5	8.1	30.6
1957	1.2	3.0	.8	7.4	33.1
1958	-.8	2.1	.6	2.3	28.7

¹ Time deposits and capital accounts.² Investments in Federal securities of U.S. Government investment accounts.³ Individuals, unincorporated business, and nonprofit institutions.

NOTE.—Components may not add to totals because of rounding.

Chart 1

Uses of Capital Funds in the Real Estate Mortgage Market, 1947-1958
(Billions of Dollars)

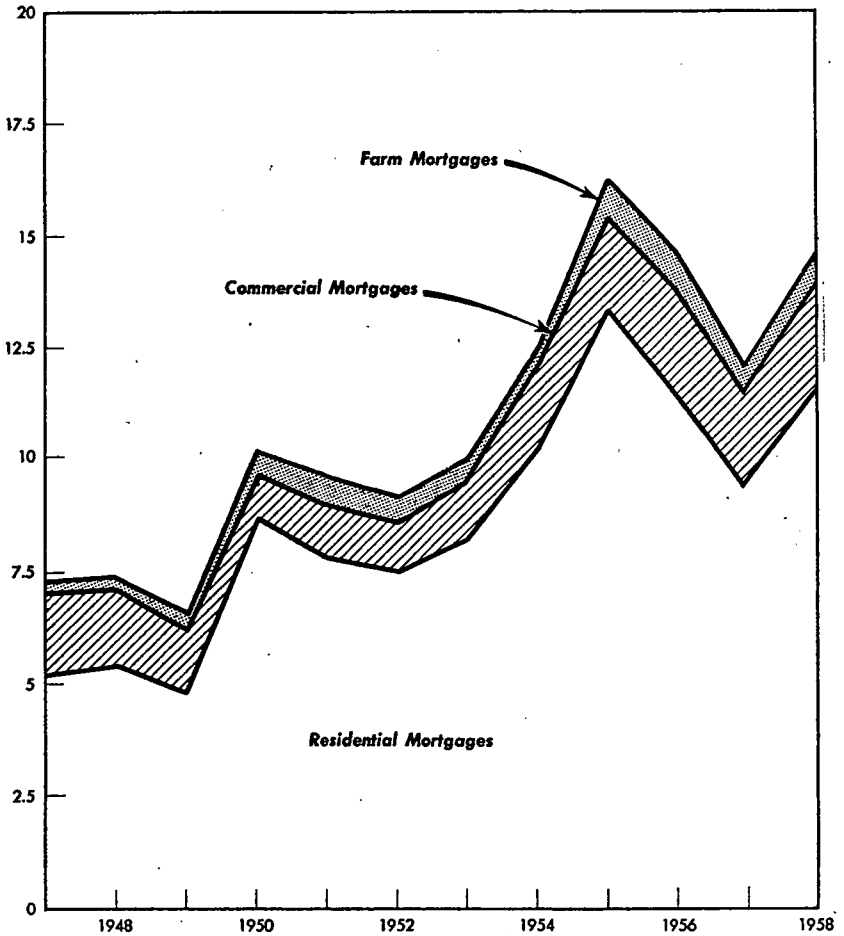


TABLE 2.—Uses of capital funds in the real estate mortgage market, 1947-58

[Billions of dollars]

Year	Residential mortgages	Commercial mortgages	Farm mortgages	Total
1947.....	5.7	1.3	0.2	7.2
1948.....	5.9	1.2	.2	7.3
1949.....	5.3	.9	.3	6.5
1950.....	8.7	.9	.5	10.1
1951.....	7.8	1.1	.6	9.5
1952.....	7.5	1.0	.6	9.1
1953.....	8.2	1.2	.5	9.9
1954.....	10.2	1.8	.5	12.5
1955.....	13.4	2.0	.8	16.2
1956.....	11.4	2.3	.8	14.5
1957.....	9.2	2.3	.6	12.1
1958 ¹	11.5	2.4	.7	14.6

¹ Preliminary.

NOTE.—Components may not add to totals because of rounding.

Chart 2

Uses of Capital Funds in Corporate Financing, 1947-1958
(Billions of Dollars)

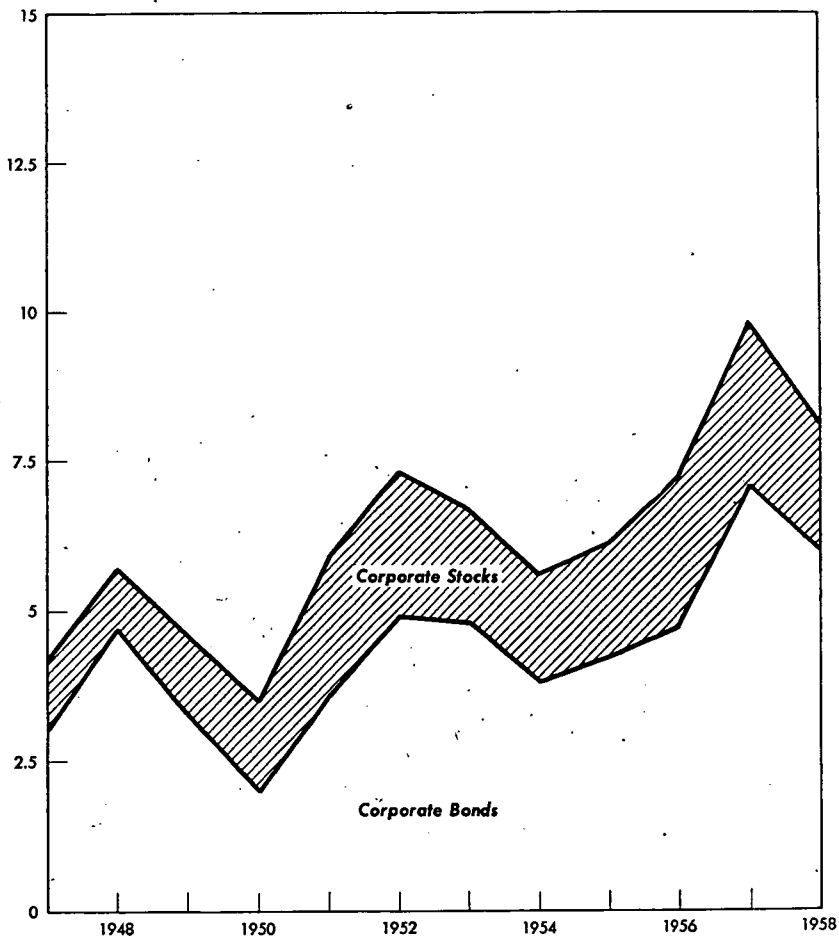


TABLE 3.—*Uses of capital funds in corporate financing, 1947-58*

[Billions of dollars]

Year	Corporate bonds	Corporate stocks	Total
1947	3.0	1.2	4.2
1948	4.7	1.1	5.7
1949	3.3	1.3	4.6
1950	2.0	1.5	3.5
1951	3.6	2.3	5.9
1952	4.9	2.4	7.3
1953	4.8	1.9	6.7
1954	3.8	1.8	5.6
1955	4.2	1.9	6.1
1956	4.7	2.5	7.2
1957	7.1	2.7	9.8
1958	6.0	2.1	8.1

NOTE.—Components may not add to totals because of rounding. Corporate stocks exclude issues of open-end investment companies.

Chart 3

Uses of Capital Funds in Residential Mortgages, Commercial Mortgages and Corporate Securities, 1947-1958
(Billions of Dollars)

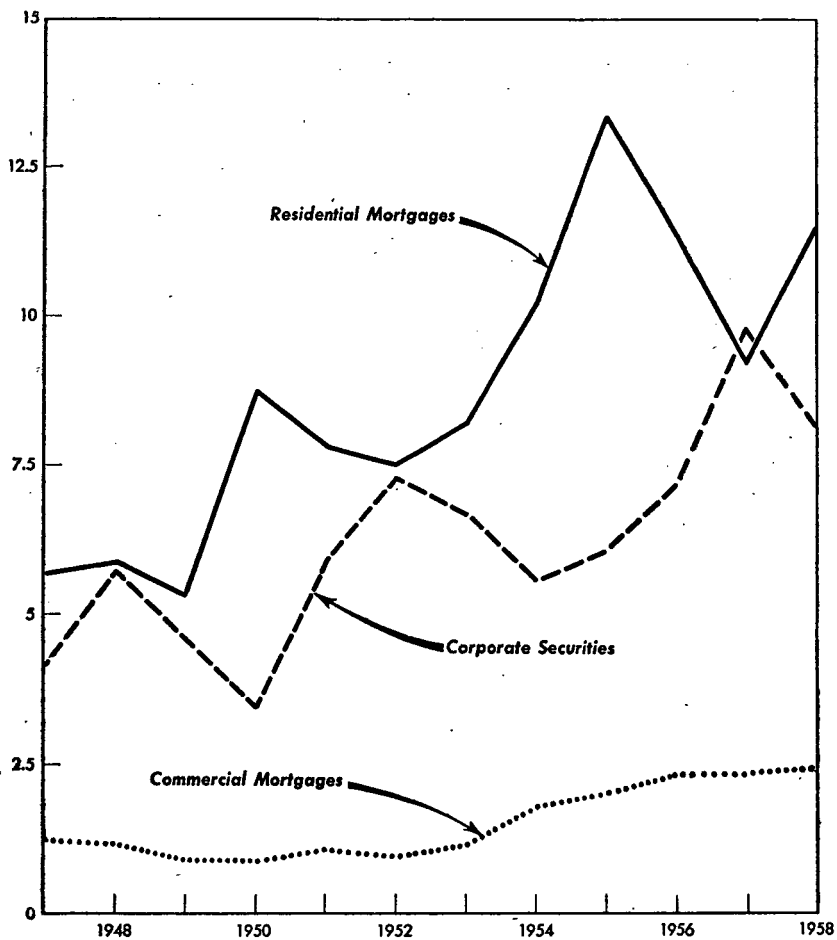


TABLE 4.—Uses of capital funds in residential mortgages, commercial mortgages, and corporate securities, 1947-58

[Billions of dollars]

Year	Residential mortgages	Commercial mortgages	Corporate securities
1947	5.7	1.3	.2
1948	5.9	1.2	5.7
1949	5.3	.9	4.6
1950	8.7	.9	3.5
1951	7.8	1.1	5.9
1952	7.5	1.0	7.3
1953	8.2	1.2	6.7
1954	10.2	1.8	5.6
1955	13.4	2.0	6.1
1956	11.4	2.3	7.2
1957	9.2	2.3	9.8
1958 ¹	11.5	2.4	8.1

¹ Preliminary.

NOTE.—Corporate securities exclude shares of open-end investment companies.

Chart 4

Uses of Funds in Government Financing, 1947-1958
(Billions of Dollars)

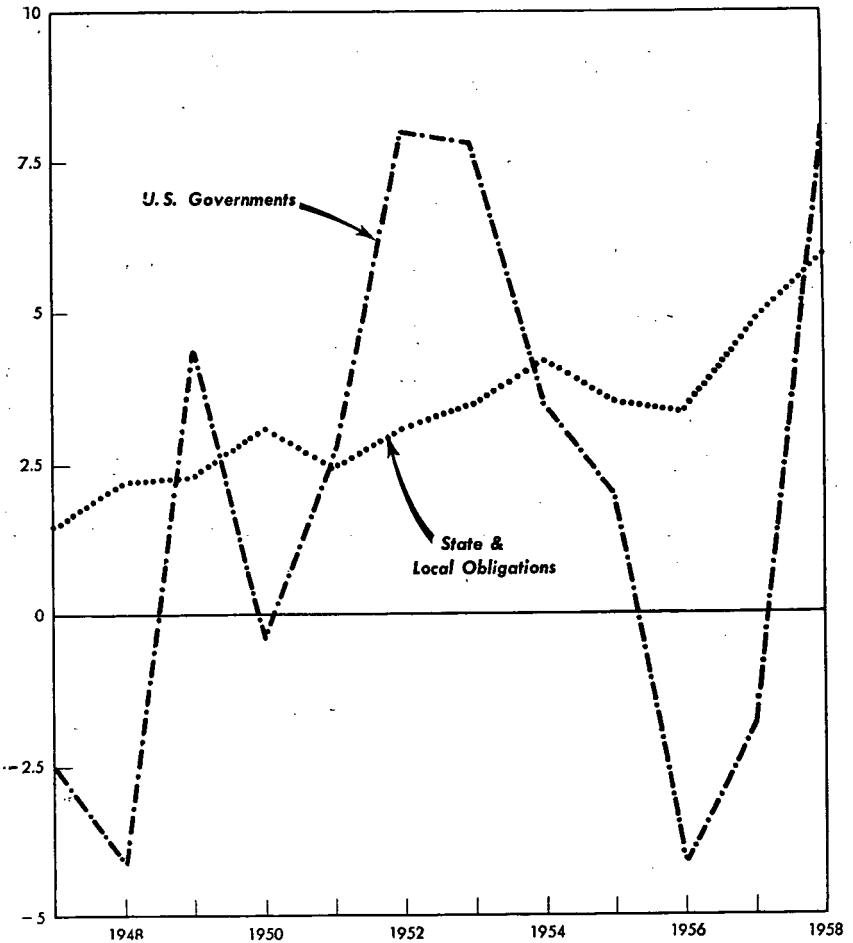


TABLE 5.—Uses of capital funds in Government financing, 1947-58

[Billions of dollars]

Year	U.S. Governments	State and local obligations
1947.....	-2.5	1.4
1948.....	-4.1	2.2
1949.....	4.3	2.3
1950.....	-4	3.1
1951.....	2.7	2.4
1952.....	8.0	3.1
1953.....	7.8	3.5
1954.....	3.5	4.2
1955.....	2.0	3.5
1956.....	-4.1	3.3
1957.....	-1.7	4.9
1958.....	8.0	5.9

TABLE 6.—Hypothetical Federal debt transactions during a year

[Billions of dollars]

Public marketable debt	Outstanding at beginning	Maturing each year	Moving into maturity class	Moving out of maturity class ¹	Added to class by new issue
Bills, 3-month.....	25	100			100
Certificates, 12-month.....	38	38			38
Total.....	63	138			138
Bonds and notes maturing:					
Within 1 year.....	12	12	12		
1 to 5 years.....	48		4	12	8
5 to 10 years.....	20		3	4	1
10 to 15 years.....	15		2	3	1
15 to 20 years.....	10		1	2	1
20 years and over.....	12			1	1
Total bonds and notes.....	117	12	22	22	12
Total marketable debt.....	180	150	22	22	150

¹ Amount outstanding in each maturity class, divided by number of years in the class. Assumes an even distribution of maturities within each class.

TABLE 7.—Long-term Treasury bonds, by type of investor, 1945-59 (due or callable in 10 years or over)

[Millions of dollars]

End of period	Commercial banks	Mutual savings banks	Life insurance companies	Fire, casualty, and marine insurance companies	U.S. Government investment accounts and Federal Reserve banks	All other investors ¹	Total outstanding	Memorandum: Corporate pension funds ²
1945.....	6,107	7,575	16,697	1,234	5,690	22,513	59,816	-----
1946.....	5,065	7,991	16,981	1,331	5,191	18,243	54,807	-----
1947.....	5,003	8,607	16,607	1,705	5,227	17,759	54,807	-----
1948.....	3,542	8,048	13,584	1,346	11,925	15,142	53,888	-----
1949.....	3,859	6,588	12,287	1,198	8,033	13,139	45,134	-----
1950.....	2,934	7,180	10,779	1,531	7,190	14,035	43,648	-----
1951.....	2,912	6,522	8,681	1,587	8,260	14,109	42,072	-----
1952.....	2,728	6,065	7,689	1,512	7,056	14,011	39,060	-----
1953.....	2,691	5,251	6,947	1,254	6,984	14,168	37,297	806
1954.....	2,243	3,056	5,183	893	6,049	12,052	29,475	644
1955.....	2,150	2,485	4,179	776	4,993	12,515	27,098	867
1956.....	1,849	1,977	3,016	635	4,121	11,883	23,484	666
1957.....	842	1,518	2,483	369	3,435	6,836	15,184	546
1958.....	833	1,608	2,680	439	3,529	7,738	16,826	526
1959-March.....	830	1,602	2,732	404	3,602	8,196	17,363	544

¹ Includes those banks and insurance companies not reporting in the Treasury survey.² Included in data for "All other investors." Data by call classes were not available prior to Dec. 31, 1953.

NOTE.—Components may not add to totals because of rounding. Data include only interest-bearing public marketable securities and investment series B bonds of 1975-80 (dated Apr. 1, 1951, offered also in May 1952) exchangeable for marketable 1½ percent 5-year Treasury notes.

Source: "Treasury Survey of Ownership," as published in Treasury Bulletin, March issue following year indicated, June issue for March 1959.

TABLE 8.—Holdings by type of investor of long-term Treasury bonds (due or callable in 10 years or over), as percent of total outstanding, 1945-59

[Percent]

End of period	Commercial banks	Mutual savings banks	Life insurance companies	Fire, casualty, and marine insurance companies	U.S. Government investment accounts and Federal Reserve banks	All other investors ¹	Total outstanding	Memorandum: Corporate pension funds ²
1945.....	10.2	12.7	27.9	2.1	9.5	37.6	100	-----
1946.....	9.2	14.6	31.0	2.4	9.5	33.3	100	-----
1947.....	9.1	15.7	30.1	3.1	9.5	32.4	100	-----
1948.....	6.6	14.9	25.8	2.5	22.1	28.1	100	-----
1949.....	8.6	14.6	27.2	2.7	17.8	29.1	100	-----
1950.....	6.7	16.4	24.7	3.5	16.5	32.2	100	-----
1951.....	6.9	15.5	20.6	3.8	19.6	33.5	100	-----
1952.....	7.0	15.5	19.7	3.9	18.1	35.9	100	-----
1953.....	7.2	14.1	18.6	3.4	18.7	38.0	100	2.2
1954.....	7.6	10.4	17.6	3.0	20.5	40.9	100	2.2
1955.....	7.9	9.2	15.4	2.9	18.4	46.2	100	3.2
1956.....	7.9	8.4	12.8	2.7	17.5	50.6	100	2.8
1957.....	3.6	10.0	16.4	2.4	22.6	45.0	100	3.6
1958.....	5.0	9.6	15.9	2.6	21.0	46.0	100	3.1
1959-March.....	4.8	9.2	15.7	2.3	20.7	47.2	100	3.1

¹ Includes those banks and insurance companies not reporting in the Treasury survey.² Included in data for "All other investors." Data by call classes were not available prior to Dec. 31, 1953.

NOTE.—Components may not add to totals because of rounding. Data include only interest-bearing public marketable securities and investment series B bonds of 1975-80 (dated Apr. 1, 1951, offered also in May 1952) exchangeable for marketable 1½ percent 5-year Treasury notes.

Source: "Treasury Survey of Ownership," as published in Treasury Bulletin, March issue following year indicated, June issue for March 1959.

Chart 5

Net Uses of Funds in Selected Investments of Mutual Savings Banks, 1947-1958
(Billions of Dollars)

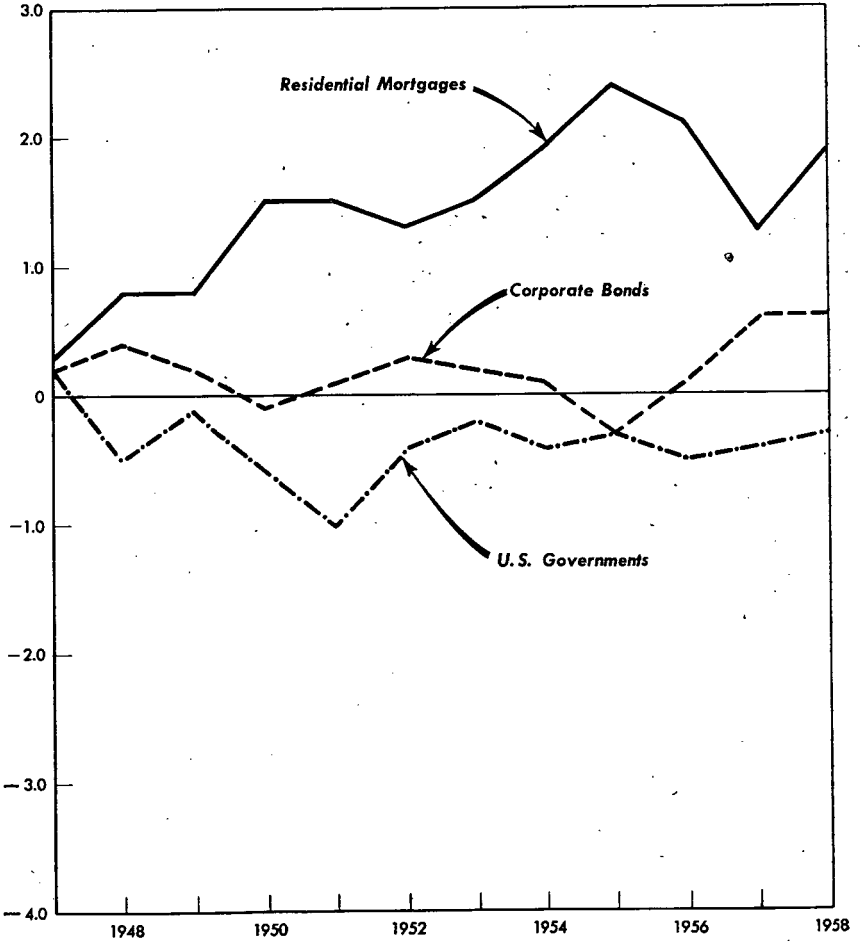


TABLE 9.—*Net uses of funds in selected investments of mutual savings banks, 1947-58*

[Billions of dollars]

Year	Residential mortgages	Corporate bonds	U.S. Governments	State and local securities
1947.....	0.3	0.3	0.2	(1)
1948.....	.8	.4	-.5	(1)
1949.....	.8	.2	(1)	(1)
1950.....	1.5	-.1	-.6	(1)
1951.....	1.5	.1	-1.0	
1952.....	1.3	.3	-.4	0.1
1953.....	1.5	.2	-.2	.2
1954.....	1.9	.1	-.4	.1
1955.....	2.4	-.3	-.3	.2
1956.....	2.1	.1	-.5	(1)
1957.....	1.3	.6	-.4	(1)
1958.....	1.9	.6	-.3	(1)

¹ Under \$50,000,000.

Chart 6

Net Uses of Funds in Selected Investments of Corporate Pension Funds, 1947-1958
(Billions of Dollars)

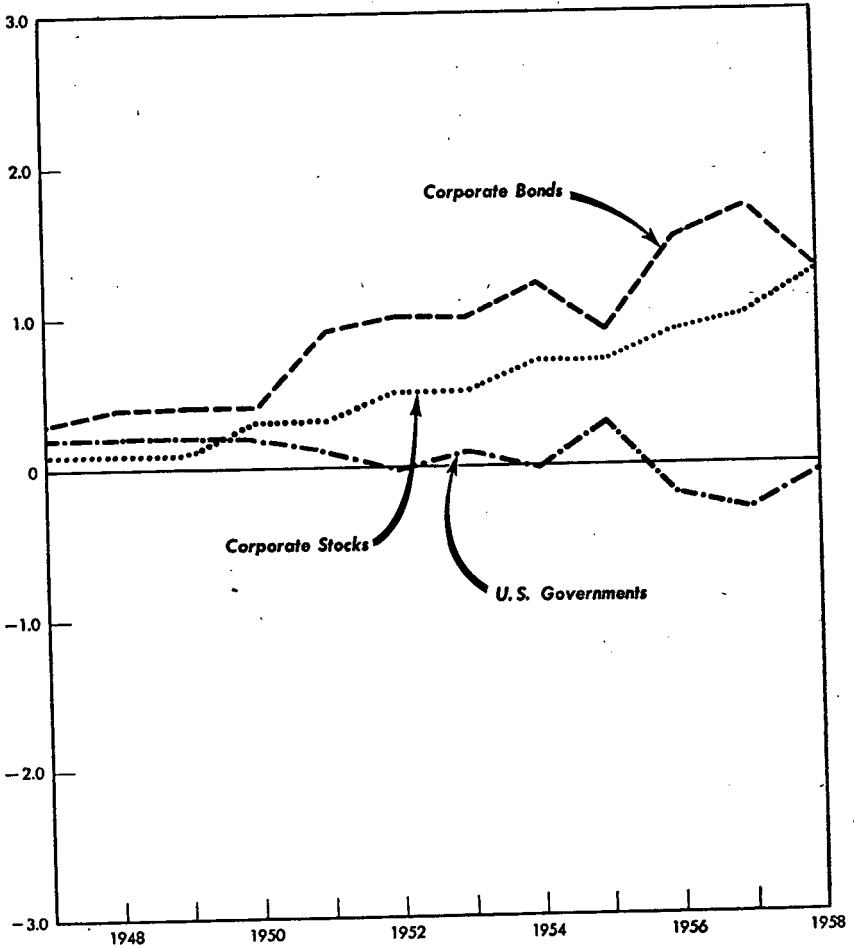


TABLE 10.—Net uses of funds in selected investments of corporate pension funds, 1947-58

[Billions of dollars]

Year	Corporate bonds	Corporate stocks	U.S. Governments	Year	Corporate bonds	Corporate stocks	U.S. Governments
1947.....	0.3	0.1	0.2	1953.....	1.0	0.5	0.1
1948.....	.4	.1	.2	1954.....	1.2	.7	(1)
1949.....	.4	.1	.2	1955.....	.9	.7	.3
1950.....	.4	.3	.2	1956.....	1.5	.9	-.2
1951.....	.9	.3	.1	1957.....	1.7	1.0	-.3
1952.....	1.0	.5	(1)	1958.....	1.3	1.3	(1)

¹ Under \$50,000,000.

Chart 7

Net Uses of Funds in Selected Investments of Life Insurance Companies, 1947-1958
(Billions of Dollars)

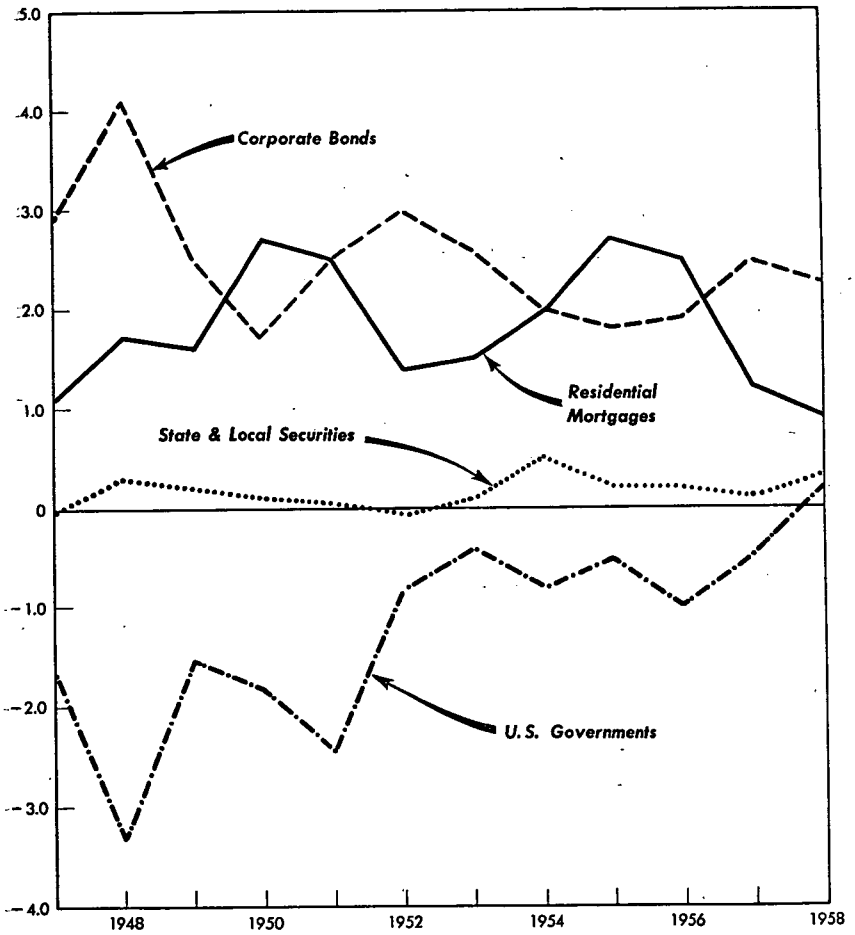


TABLE 11.—*Net uses of funds in selected investments of life insurance companies, 1947-58*

[Billions of dollars]

Year	Residential mortgages	Corporate bonds	U.S. Governments	State and local securities
1947.....	1.1	2.9	-1.6	(1)-
1948.....	1.7	4.1	-3.3	0.3
1949.....	1.6	2.5	-1.5	.2
1950.....	2.7	1.7	-1.8	.1
1951.....	2.5	2.5	-2.4	(1)
1952.....	1.4	3.0	-7.8	(1)
1953.....	1.5	2.6	-4	.1
1954.....	2.0	2.0	-8	.5
1955.....	2.7	1.8	-5	.2
1956.....	2.5	1.9	-1.0	.2
1957.....	1.2	2.4	-5	.1
1958.....	.9	2.2	.2	.3

1 Under \$50,000,000.

TABLE 12.—*Comparative yields on U.S. savings bonds, marketable bonds, and savings deposits*

	Annual averages					June 1959
	1941	1945	1948	1952	1958	
Savings bonds: ¹						
Series E.....	2.90	2.90	2.90	3.00	3.26	3.26
Series H.....				3.00	3.26	3.26
Series F.....	2.53	2.53	2.53	(2)	(2)	(2)
Series J.....				2.76	(2)	(2)
Series G.....	2.50	2.50	2.50	(2)	(2)	(2)
Series K.....				2.76	(2)	(2)
Marketable bonds:						
U.S. Government long-term.....	2.37	2.37	2.44	2.68	3.43	4.09
Moody's AAA corporate.....	2.77	2.62	2.82	2.96	3.79	4.46
Deposits and shares:						
Savings banks deposits.....	1.89	1.68	1.78	2.43	3.17	(3)
Savings and loan shares.....	3.10	2.50	2.30	2.80	3.50	(3)
Commercial bank savings deposits.....	1.30	.80	.90	1.10	2.30	(3)

1 Yield per annum if held to maturity.

2 Issuance discontinued in May 1952.

3 Issuance discontinued in May 1957.

4 Average yield for month of December 1941.

5 Not available.

MR. CONKLIN. I am George T. Conklin, Jr., vice president (finance), the Guardian Life Insurance Co. of America, New York City. Accompanying me are Sherwin C. Badger, financial vice president, New England Mutual Life Insurance Co., Boston; James J. O'Leary, director of economic research, Life Insurance Association of America, New York City; Robert B. Patrick, vice president, Bankers Life Co., Des Moines; and Richard K. Paynter, chairman of the finance committee and executive vice president, New York Life Insurance Co., New York City. We are glad to have the opportunity to take part in these important hearings on the Government's management of its monetary, fiscal, and debt operations. We have prepared a detailed statement which I would like to submit to be a part of the record. With your permission, I shall proceed by reading a summary of the statement, and then my associates will join me in discussing any questions the committee may want to raise.

I should like to make clear that this statement represents my views and those of my associates, and is not an official statement of the views

of the life insurance industry, though I would hazard a guess that it would be generally endorsed by many in the industry.

I will turn now, with your permission, to the summary of the statement in the interest of economy of time as suggested by you, Senator Douglas.

Summary and conclusions: The ability of the U.S. Treasury to conduct its financing and debt management operations on a wise basis is of crucial importance for the attainment of our national goals of full employment, sustainable economic growth, and general price stability. There is hardly any other matter of greater importance to the country today than that the U.S. Government be able to finance itself and manage the Federal debt in a manner consistent with these objectives. Accordingly this statement is focused on the Treasury's financial and debt management problems, with monetary and fiscal policy questions considered within this focus.

Regarding the objectives of national economic policy we believe that full employment, sustainable economic growth, and general price stability are vitally interdependent in the longer run, and that all three objectives must be pursued as a whole if we are to preserve our free economic society. This is because a national policy of inflation—even "creeping inflation"—would have destructive consequences for economic growth and economic and political democracy, as follows: (a) A continued decline in the value of the dollar is bound to injure and eventually destroy the willingness of the American people to save voluntarily and thereby to provide the only sound means of financing economic growth. Under our economic system the growth process springs from the willingness of the people to save some of their income and the investment of these savings in factories, mines, business concerns, homes, public works, and other capital goods, as well as working capital. (b) The decreasing willingness of the American people to buy Government bonds either directly or through savings institutions as the general price level rises accentuates the U.S. Treasury's financing problems and leads to the issuance of a larger and larger portion of short-term debt thus making inflation more difficult to control. (c) A persistent inflation is bound to breed a multiplicity of Government controls and ultimately to place serious curbs on our free market economy and thus on our economic and political freedom.

During the postwar period the ability of the U.S. Treasury to sell long-term bonds has been reduced sharply and the problem of maintaining a balanced maturity distribution has become more and more difficult. In no small measure this is because of the repeated Federal deficits which forced the Treasury to borrow in 7 of the 12 years, 1947-58, for a huge total of over \$36 billion. It is also because of the enormous competing demands for capital funds in the private sectors of the economy and for State and local financing which, along with Federal financing, too often have exceeded the total supply of savings. These competing private demands, encouraged and even stimulated by Government housing and tax policies, have been able to outbid the U.S. Treasury in obtaining the available funds. The inflation engendered by an expansion of the supply of money to supplement savings, along with the wage-price spiral, has itself made it more difficult to sell long-term Treasury bonds.

Our review of the Treasury financing and debt management in the perspective of the capital market and the national economy as a whole in the postwar period suggests that the following basic steps must be taken if the market for Government bonds is to be broadened:

(a) The Federal Government and the Congress must together concentrate vigorously with all fiscal, monetary, and other appropriate policies to bring an end to inflation and to destroy the psychology of inflation. Sound Government financing requires that in periods of high prosperity the Federal Government should run a budgetary surplus and should retire some of the debt. Further, the Employment Act of 1946 should be amended to make it clear that general price level stability is a goal of equal importance with full employment and economic growth.

(b) Foremost in the fight against inflation, we need better understanding of the fact that the only source of real growth in our national economy is saving and the investment of savings in capital goods. As a country we have been attempting to grow faster than our national saving justified. Too often we have resorted to the creation of money to finance the growth beyond what we have been able to finance through savings. We have learned the painful lesson that capital expenditures financed by an increase of the money supply under boom conditions are the certain way to inflation.

(c) Careful attention must be given to reforms of the Federal tax system which would encourage saving. In view of the shortage of savings relative to the demand for capital funds which has characterized the postwar period, and which will continue in the foreseeable future, our tax system needs to be subjected to careful study to eliminate forms of taxation which unnecessarily discourage saving. This is not an easy task, in view of the heavy revenue needs of the Government, but the need is clear in terms of the great demands ahead for capital funds. Toward the same end, interest rate policies of the Federal Government should be reexamined to see if they are consistent with the requirement of greater savings.

(d) The only possible way for the Treasury to raise long-term funds on a sound basis in a free capital market is to pay the interest rate required to bid funds away from other users. The Treasury task of bidding for long-term funds will be eased to the extent that steps outlined in the foregoing three parts of this summary are carried out.

The principal conclusions reached in this statement regarding several specific questions of Federal financing and debt management are as follows:

(a) Debt management should not be regarded as an important tool to be employed by the Government in combating the business cycle. Government efforts to counteract the cycle have much greater potentialities in the area of monetary and fiscal policy. The objective of lengthening the average maturity of the Federal debt has proved so elusive, yet is so important, that the Treasury should be alert to the opportunity of selling long-term bonds even in periods of general business slack. If there is an accumulation of long-term funds available to purchase Government bonds, the Treasury should make such bonds available even though a business recession may exist. If such sales do seem to interfere with business recovery, monetary measures can be used to aid in correcting the situation.

(b) Treasury financing and debt-management operations should be aimed primarily at developing a balanced maturity distribution of the debt, with a substantial proportion of the debt in intermediate and longer-term issues. Such a maturity distribution would have important advantages for the Treasury, the capital market, the monetary authorities, and the economy as a whole. In particular, from the standpoint of the Federal Reserve and the objective of sustainable economic growth without inflation, an orderly spacing of maturities and a reduced frequency and size of refunding operations would allow far greater freedom to pursue credit policies consistently.

(c) In order to bring nonbank investors such as mutual savings banks, uninsured pension funds, and life insurance companies back into the Government bond market as net purchasers, the all-important step is for the Treasury to offer an interest return fully competitive with the yield available on other investments such as residential and commercial mortgages and directly placed corporate bonds. In addition, it is desirable that nonbank investors be permitted to pay for Government bonds on a deferred basis. This would permit such investors to fit their purchases into their forward commitment picture and their cash-flow expectations.

(d) The Treasury should give serious consideration to advance funding of some portion of the debt which has come into the shorter maturity ranges. The investment series B bonds would present a good possibility for advance funding. In addition, the Treasury should consider the desirability of combining an advance funding operation with a cash offering of a long-term bond.

(e) The Treasury should seriously consider offering incentives to the securities business to sell long-term marketable bonds. This means that the Treasury should consider paying commissions to brokers and dealers just as is done in the marketing of private securities.

(f) In order to encourage the purchase of U.S. savings bonds, the interest return on such bonds should be raised in line with the return on private investments. In addition, the Treasury should also provide a system of incentives to the securities market to promote the sale of savings bonds. A tax-exemption feature should also be considered.

(g) It would be a serious mistake, to say the least, for the Treasury to introduce a "purchasing power bond" in which the amount paid at maturity (or the amount of interest) is tied to some price index such as the index of consumers' prices. This would be tantamount to admission of defeat in the struggle to halt inflation.

The decline which has occurred in the prices of Government bonds during the past year has revived the argument that the Federal Reserve, through open market purchases, should support the prices of Government securities. A return to the policy of Federal Reserve pegging of the prices of Government bonds, as followed in the decade prior to March 1951, would be disastrous in that it would place our country on the road to ruinous runaway inflation. It would force the monetary authorities to foster an uncontrolled expansion of our money supply, thus promoting a sharp and accelerating rise in the cost of living, and would actually drive up interest rates on all other forms of debt except Government securities.

Some who recognize the disastrous consequences of a pegging operation suggest that, as the occasion demands, the Federal Reserve

should buy longer term Government securities to afford stability to long-term rates, and at the same time sell an offsetting amount of short-term securities to prevent any net addition to commercial bank reserves and hence the money supply. Such an operation would have no effect on the general level of interest rates, but it would hold down the yields on longer term Government securities and raise the rates on short-term issues. Higher interest costs to the Treasury on short-term issues are quickly translated into a higher service charge on the Federal debt because \$76 billion of Government securities mature in 1 year or less. Moreover, Federal Reserve support of longer term Government bond prices would lead to a rapidly increasing volume of sales of such securities by private investors, and the outcome eventually would be that the Federal Reserve would wind up holding most of the long-term Government bonds, and short-term interest rates would be driven to a very high level, with the service charge on the Federal debt much higher in the process because of the huge volume of short-term debt.

If the Federal Reserve is to retain its freedom to restrain the expansion of the money supply in a period of high and rising economic activity, which we believe is absolutely essential, there are no manipulations of open market operations that can escape the discipline of demand and supply forces in the capital markets.

Mr. Chairman, that completes the reading of the summary. With your permission we would like to have any member of the panel join in the answering of the questions as he may see fit.

The CHAIRMAN. Thank you very much. It is in a nonmischievous spirit that I ask the following question. I think you properly emphasize the desirability of not merely a balanced budget, but a surplus, which can be used to retire a portion of the public debt. You therefore would favor an increase in taxes in such periods as this, would you?

Mr. CONKLIN. I am sorry, I could not hear that.

The CHAIRMAN. You would favor an increase in taxes to increase governmental revenues in a period of revival so that a portion of the public debt could be retired, and thus stability introduced in the fiscal affairs?

Mr. CONKLIN. I would rather examine the extent to which Government expenditures could possibly be reduced to achieve the same objective.

The CHAIRMAN. Would you favor plugging loopholes in the tax system?

Mr. CONKLIN. I would certainly favor plugging any loopholes in the tax system, as a general principle.

The CHAIRMAN. In the past the life insurance industry or the insurance industry as such has had one of the lowest rates of taxation of any industry, so I take it you are in favor of the action of the Finance Committee in increasing the taxation of insurance companies particularly on profits made from underwriting and which raise total receipts or will raise total receipts from the insurance industry from roughly \$300 million to roughly \$500 million a year?

Mr. PATRICK. Senator, are you speaking accurately when you say we have the lowest rate?

The CHAIRMAN. That is on net income. It is one of the lowest rates of taxation on net income. 52 percent and 15 percent of the income. This applies not merely on mutual, but to stock companies as well.

Mr. CONKLIN. I would like to state that the life insurance industry in the United States, which is to a substantial extent, as you are aware, a savings institution, is the most heavily taxed savings institution in the world.

The CHAIRMAN. Is this true in the case of stock companies where the profits accrue to the holders of stock rather than being returned to the holders of policies?

Mr. CONKLIN. I am speaking of the overall picture.

The CHAIRMAN. I am speaking to stock companies. Would you oppose the increase in taxation to stock companies?

Mr. CONKLIN. That has been done.

The CHAIRMAN. Would you favor a further increase?

Mr. CONKLIN. No; I would not.

The CHAIRMAN. Here is one of the difficulties we get into. People speak of the desirability of increasing governmental revenues and plugging loopholes, but no one will admit that they are in possession of a loophole. So Congress has always been berated for not closing somebody else's loophole. I merely raise this point and pass on.

I would like to address a question of your paper in which you say that the level of interest rates has an important influence on the willingness of people to save. Do I take it that you assume that an increase in the interest rate will increase the rate of savings?

Mr. CONKLIN. Yes. This is a difficult fact to statistically prove. I believe that the tendency is for an increase in interest rates to increase savings.

The CHAIRMAN. I may say 35 years ago I believe that, too, because I assumed that savings were positively inclined. Then I spent 2 years studying this subject, 1 year studying the writings of the various economists on the subject, and I found they made every assumption under the sun from negative supply curves of savings to positive supply curves, to constant rates, to first up and down rates, and so forth. Then I spent a year studying the statistics. I could find absolutely no connection between changes in interest rates and changes in the rate of savings. That was 30 years ago. I published the results in a chapter of a book that I wrote. Have you later information to prove that an increase in the interest rate increases the rate of savings?

Mr. CONKLIN. I don't believe it would be possible to demonstrate a close correlation, Senator, between minor changes in interest rates and savings. I do believe, however, that there can be a very substantial effect upon savings of large changes in interest rates.

The CHAIRMAN. That is to raise the interest rate to 8 percent?

Mr. CONKLIN. No; this is not the question. The question is possibly whether the attempt to depress interest rates to extraordinarily low levels would not tend to reduce savings.

Mr. O'LEARY. May I just add this thought? One of the very noticeable things in the savings picture is that if you get an increase in interest rates on savings bank deposits versus the interest rate on commercial bank time deposits, there are very sharp movements of funds from commercial bank time deposits into the savings bank field.

Whatever institution happens to get into the lead in terms of the rate it is paying, whether it is a savings and loan, or a savings bank, there are pronounced shifts of funds as between institutions. This proves that savers are sensitive to rate changes. It does not prove that changes in the interest rates will affect the total volume of savings, although this may be true.

The CHAIRMAN. That is not the point I wanted to raise.

Mr. O'LEARY. However, I think it does at least give you a clue to the fact that the interest rate is a very important factor in attracting savings as between the various types of institutions.

The CHAIRMAN. I don't doubt that at all.

The raise in the interest rates by one set of savings institutions will draw savings to it. This advantage will be someone else's disadvantage. The question is whether the increase in interest rates gives society more savings.

Mr. O'LEARY. As you know, Senator Douglas, the statistics we have on savings as prepared by the Department of Commerce and others are largely residual figures growing out of the GNP figures, and so forth, and they are not very good figures on savings.

The CHAIRMAN. They are the best figures we have.

Mr. O'LEARY. They are the best figures we have but it is awfully hard to use them with precision. If you take the Goldsmith "Study of Savings," it tends to show that the rate of saving, as related to disposable income, has been constant over a long period of time. However, Goldsmith himself has 200 pages of footnotes indicating the weakness of the savings figures.

The CHAIRMAN. No matter what the interest rate may be, the percentage of savings from the gross national product, as you say, tends to remain the same, despite an upward drift in the real income.

Mr. O'LEARY. All I am suggesting is that perhaps some light is being shed on this question by the speed with which funds shift as between various forms with changes in interest rates.

The CHAIRMAN. I don't doubt that for a minute. The question is, taking the economy as a whole, whether an increase in the interest rate raises the total volume of savings. I think what you have said bears out my own judgment that there is absolutely no statistical evidence to support this. This is an article of faith, a faith which I held once very strongly, but about which I have become somewhat dubious.

Mr. O'LEARY. I think there is a good deal to what you say. I was merely trying to add that particular piece of evidence which I think has a bearing.

Mr. PAYNTER. May I add this one thing? I am sure you cannot prove it on the upside, although many of us believe it. I do think there is a negative point on the downside. There is a certain rate below which people say "Oh, what the heck," and would rather spend it than keep it.

The CHAIRMAN. That may well be true. There are those who argue that since a person wants to set aside a certain amount for an annuity or get a certain yield, if the rate goes down he will save more in order to get the same yield.

Mr. PAYNTER. It is sometimes hard to do, sir.

The CHAIRMAN. I know.

Now, let me turn, if I may, to a more technical question in the field of debt management. The American Bankers Association and the Investment Bankers Association are commonly called into conference with the Treasury when they make a new issue of either short-term or long-term Government securities. Are you frequently called into conference with them?

Mr. CONKLIN. We are on occasion called in to discuss it with them. The CHAIRMAN. When was the last time you were called in?

Mr. O'LEARY. It was the end of April.

The CHAIRMAN. Can you recall offhand how many times you have been called into conference in the last 4 years?

Mr. O'LEARY. I would say in the last 4 years we have probably averaged about three times a year.

The CHAIRMAN. So you have been called into conference 12 times.

Mr. O'LEARY. That is right.

The CHAIRMAN. Have you made a record of the recommendations which you make at these conferences?

Mr. O'LEARY. We never made any specific recommendations. Our procedure, Senator Douglas, is quite different from that followed by the ABA or IBA. I was present at the hearings before the select committee, and I have heard their testimony. Their procedure is a much more formal one than ours. We have been meeting with the Treasury in an advisory capacity since 1941. I have been in my present job since 1946. My first recollection of these meetings is that we met with Secretary Snyder. The procedure is a very simple one and has changed little over this period. When we get to the Treasury we are presented with a slide show. This slide show brings together the basic data you can find in the Treasury bulletin but it brings it together in a well coordinated form to give us a picture of the Treasury's current situation.

Then following that we have a discussion of about an hour with the Treasury and so far as we have been useful, and I have some reservations as to how useful we have been to the Treasury, our function has been merely to provide a sounding board to them as to what the current status of the capital market is—how we see the capital market. They have been interested in knowing how we see the mortgage market, both VA and FHA. They have been interested in the corporate bond market. Their basic purpose has been to try to find out what are the conditions in the capital market with reference to whether the Treasury might have an opportunity to sell a long bond. We have never made a specific recommendation. The procedure has been one in which, when we have gotten through, there has been some conclusion reached as to whether there might be some funds around to buy a long bond. There lots of times has been a discussion as to whether we might have an interest in buying such a bond. It has been mainly just a kind of sounding board type of operation.

The CHAIRMAN. In other words, you do not make recommendations either as to the rate of interest or the length of the issue.

Mr. O'LEARY. That is right.

The CHAIRMAN. But the ABA and the IBA do.

Mr. O'LEARY. All I know about their procedure is the testimony that they presented, which, I believe—it is a matter of record—they did make definite recommendations. They have a very formal procedure which has also been developed over a period of time.

The CHAIRMAN. May I ask the staff if the ABA has presented its additional recommendations since the period 1956? I am told not. It is in the mails, but it has not yet arrived.

Some of us have suggested that instead of this process of dealing with representatives of savings institutions, which I call a negotiated rate or a collective bargained rate—I don't know that the Treasury would accept those terms—some of us have urged that an alternative policy be developed in which the auction is used and that there be competitive bidding for new issues of Treasury securities. I may say this in connection with this as I have read the Joint Report of the Treasury and the Federal Reserve, they misunderstood the nature of our proposal. They thought we were speaking of an auctioning system after the issue had occurred. I am suggesting an auctioning system at the time of issuance in which the Treasury would fix the interest rate and the duration. Then the bidding would be on the basis of price. Adequate time should be given for various savings and lending institutions to become acquainted with the terms of the issue.

Have you formed any opinion on that?

Mr. PATRICK. Is it similar to the process used in auctioning bills in which each individual investor names his own price?

The CHAIRMAN. Yes.

Mr. PATRICK. Or similar to what is done in the municipal market where syndicates are formed which buy the whole issue.

The CHAIRMAN. I am not familiar with the municipal market. At the same time we hope it would not be restricted to 17 dealers. We would want a very broad market. We hope that you people might come into it.

Mr. PATRICK. In other words, somebody might bid 4.5 percent and somebody 4.55 and somebody else 4.60, and if the Treasury had a billion dollars worth to sell, it would pick out the billion at the lowest rates and sell them.

The CHAIRMAN. Yes.

Mr. PATRICK. I would see no objection to that, giving my personal reaction.

The CHAIRMAN. It would let you into this market where you are now largely excluded; isn't that true?

Mr. PATRICK. Not excluded.

The CHAIRMAN. From which you voluntarily more or less retire; isn't that true?

Mr. CONKLIN. Mr. Chairman, speaking as a financial officer and just for myself, my conviction has been that the U.S. Treasury has failed almost always to come up with a rate which is competitive and attractive to us. Therefore, far from being a negotiated rate, which is a giveaway rate or an attractive rate, we have felt it is very unattractive. For that reason I feel I would be more than happy to see an auction market which would reflect the forces of supply and demand. I feel that then the Treasury bonds would be offered on a realistic market basis, and much more attractive.

As to how this would be feasible or whether it would be feasible or not, that would be another question. I certainly would have no objection to this in principle.

The CHAIRMAN. Of course, we have met with very great resistance from both the Treasury and Federal Reserve on this, but I am very glad to get your testimony, because it seems to me to be very sound.

Mr. PATRICK. Did they understand it? They are doing it in bills.

The CHAIRMAN. They understand it thoroughly.

Mr. PAYNTER. I would warn you, sir, that I think it would produce a materially higher rate, as Mr. Conklin has said.

The CHAIRMAN. I am not so certain about that. I am not at all certain.

Mr. PAYNTER. There certainly is no objection to trying the procedure.

Mr. O'LEARY. One thing that is true is that you would very likely get a wide spread in the bids. For example, if the Treasury put up a billion dollars of long bonds—say 30-year bonds at 4¼-percent rate—the dispersion of the bids might be very great. For example, State and local funds might be willing to bid part for it, but State and local funds might not be in a position to take more than \$200 million of the issue. Then you could go all the way down the line to other investors who would have alternative places to put their money, VA, and FHA mortgages, conventional mortgages, who might bid only 90 for it. So you would have a very wide spread in order to sell the entire issue.

The CHAIRMAN. The Treasury would have to know how much to issue, and not issue more than the market could absorb at a reasonably competitive rate of interest.

Mr. O'LEARY. That is true. That is one of the reasons why they have these advisory committees, because it is of such key importance to them to try to find out how much money might be available. That is the way they have used us in particular, I might add.

The CHAIRMAN. Would not your companies and other institutional investors be more likely to buy Treasury securities if these bond offerings were made more frequently and more regularly, say every month, and in relatively small amounts?

Mr. BADGER. No, sir. I think it is a question not of the frequency of offerings, but with us it is purely a question of rate and competitive alternative outlets for our funds.

The CHAIRMAN. Do you favor the auction technique which I suggested?

Mr. BADGER. I think it would be interesting to try it. How it would work out in practice after the first time I haven't the faintest notion.

The CHAIRMAN. One of the objections that the Treasury advanced is that there are not enough experts in Government bonds and that lenders would suffer.

Mr. BADGER. I don't quite follow that.

The CHAIRMAN. Don't your companies have quite skilled experts in this field?

Mr. O'LEARY. My impression of that is that grew out of a misunderstanding on the part of the Treasury as to what you meant by an auction market. They were thinking of the municipal bond or public utility auctions. I think their point was that there would be just one or two bidders. There would be a scarcity of professionals. If it were clear to the Treasury that the auction market process would be

the way we have described it this morning, certainly there are hundreds of financial officers in the life insurance business who would have an ability to bid on these bonds.

The CHAIRMAN. Other institutions and mutual savings.

Mr. BADGER. Yes. I think there may have been a misunderstanding that what you were talking about was competitive bidding. You obviously could not get syndicates of a size large enough to handle large Treasury offerings.

The CHAIRMAN. I appreciate your desire to protect the Federal Reserve and Treasury, but we tried to make it abundantly clear what we were proposing.

Mr. CONKLIN. It is not a case of trying to protect anybody. We were confused by the issue some time ago when we were discussing it among ourselves, and the question was just what an auction market meant. Several of the people initially reacted unfavorably. I think that it reflects the auction type of market as in the bill market and we would have no objection to that in principle. The only reservation we would have is whether it might be feasible in operation.

The CHAIRMAN. I have exhausted my time. Mr. Patman.

Representative PATMAN. Gentlemen, you have presented a most helpful paper, and I think it was very good of you to come down and give us the benefit of your experience.

Mr. O'Leary gave us wonderful cooperation in the House Small Business Committee when we were considering the Small Business Investment Act. I know you gentlemen all cooperated, too, because you gave us a lot of factual information about your portfolios and other matters.

I would like to take advantage of your first hand experience to learn about the operations of a securities market and the part our great financial institutions play. So if I may, I would like to ask some questions which may seem personal, though I do not mean them to be personal. If I ask questions you prefer not to answer, I won't insist on an answer.

Mr. Conklin, let me ask you a couple of questions on points that your statement brings out. Is there any real difference in risk as between a Government bond and a Government guaranteed FHA or VA mortgage?

Mr. CONKLIN. Yes, I would say there is a definite difference in risk, but that difference has been interpreted in the market to be less and less.

Representative PATMAN. Experience has taught you, has it not, that it really does not make any difference?

Mr. PATRICK. It makes some difference.

Mr. CONKLIN. I would not say it does not make any difference. The market has come to view it as being a small difference.

Representative PATMAN. I recall in your statement a while ago that you stated that the Government market should be fully competitive in the sale of Government securities.

Mr. CONKLIN. Yes, absolutely.

Representative PATMAN. To the extent that it would even be competitive with housing mortgages, I understood you to say.

Mr. CONKLIN. I would mean that it would be competitive with any other alternative use of savings.

Representative PATMAN. Yes, sir.

Mr. BADGER. May I insert a comment?

Representative PATMAN. Certainly.

Mr. BADGER. I don't think that Mr. Conklin meant that the only point of competition is the rate. There are other things such as marketability, the fact that a long-term Government bond is nonrefundable, and various other things. There is more than rate that means competition.

Representative PATMAN. I see. So the phrase "fully competitive" means a number of things.

Mr. BADGER. That is right.

Representative PATMAN. You say in your statement that rates of Government bonds must be made fully competitive with the yields on other investments. I believe you point out that you can readily buy $5\frac{1}{4}$ percent mortgages at a price of 96 to produce $5\frac{3}{4}$ percent. Do you feel that to convert the debt to long term, that to sell 12 year bonds at $5\frac{3}{4}$ percent is about as high as the Treasury would have to go?

Mr. CONKLIN. This is a difficult question to answer. I don't think there would be any direct comparison that you could make; the market would have to be tested out. What exact rate it would take for a bond of that kind I would not care to hazard an offhand guess.

Mr. O'LEARY. May I make a technical correction, Mr. Patman?

Representative PATMAN. Certainly.

Mr. O'LEARY. In our testimony we pointed out, and I can appreciate your being confused about this, the gross rate of interest on an FHA mortgage is $5\frac{3}{4}$ percent, but the net to investors after all costs, servicing costs, and home office costs, gives about 5 percent. That is a rough figure. There are three-quarters of 1 percent of cost that are involved. So even if you can get gross $5\frac{3}{4}$ on an FHA, what the Treasury would be competing with is a net rate of 5 percent, because there are so little costs on administering the Government bond portfolio. So your figures should be comparing the Government rate with the net rate on the FHA mortgages after cost.

Mr. CONKLIN. Mr. Patman, was that $5\frac{3}{4}$ percent interest you mentioned?

Representative PATMAN. Yes.

Mr. CONKLIN. I thought you said $4\frac{3}{4}$ percent. It would certainly not take a rate as high as $5\frac{3}{4}$ percent for a long Government bond to be competitive at present, for some large corporate issues are placed at 5 to $5\frac{1}{4}$ percent currently.

Representative PATMAN. Now, about the inflationary psychology you discussed and the flight of savings from fixed return securities, that applies to the purchase of life insurance, too. It applies to life insurance as well?

Mr. CONKLIN. Yes, sir.

Representative PATMAN. Has the inflation caused any real decline in life insurance sales?

Mr. PAYNTER. I have some figures here, sir, from our own experience. Would you like to hear them?

Representative PATMAN. On this point of declining sales?

Mr. PAYNTER. About the change in the character. May I make it very simple?

Representative PATMAN. Yes.

Mr. PAYNTER. In 1946 my company did about 8 percent of its total business in term insurance or in policies having a term element. Today the term element in our business has risen to 25 percent of our business.

Representative PATMAN. That is due to the fear of inflation. That is part of it.

Mr. PAYNTER. That we believe is one of the important factors.

Mr. PATRICK. Mr. Patman, I would like to say that fear of inflation is one thing our sales force is experiencing more and more from well-informed buyers. They desire to buy term insurance because of the small element of savings involved. They are telling our salesmen that they are using savings to buy equities of one type or another.

Representative PATMAN. That leads me to ask this question, Mr. Patrick. The first part of the year the life insurance companies engaged in quite a terrific campaign against inflation at a time when I did not think we had any inflation except high interest inflation. I just wonder if that affected your sales and that caused you to kind of pull back and stop your advertising.

Mr. PATRICK. I am afraid this is a much longer term thing than just what happened in the last few months. Our program of discussing inflation in the public press is a public relations matter. It springs from a very serious concern on our part about inflation.

Representative PATMAN. That is a great public service the life insurance companies render. I know during the war you rendered a great public service.

Mr. PATRICK. We hope we are rendering a great public service.

Representative PATMAN. I know you intend to do that. I wonder if it did not react against you in the early part of the year? I believe I noticed that you retreated and pulled your horns in a little bit. Am I correct about that, or not, Mr. O'Leary?

Mr. O'LEARY. I don't have anything to do with this advertising campaign on inflation so I cannot be too authoritative about this, but I did see one of the ads the other day in the newspaper and as far as I know the campaign is continuing.

One thing I think should be pointed out is that it may surprise you to know that there are 112 million people in this country who have life insurance policies, and the total value of life insurance is over \$500 billion. I think if any of us were sitting in the chair of an executive of a life insurance company and saw over the last 12 years the value of the proceeds of life insurance hit by inflation as they have been hit, you would get kind of excited about this inflation.

We have tried to acquaint the public with what has happened. That is the origin of this program. I think if anything we perhaps have not done enough to acquaint the public with the effects of this inflationary process.

Representative PATMAN. I am not taking issue with you. I think it is a fine thing to alert the people against inflation. At the same time when there is no inflation going on, I think it could be a disservice to the country.

Mr. O'LEARY. That is a question. When you say there is no inflation going on, it is true that the indexes of prices, the wholesale commodity price index or the Consumer Price Index are at present

perfectly level. But we feel whether the indexes of prices are perfectly level is not really the important thing at this time. We feel the important thing has been that the American people have become convinced that inflation is something that is going to be with us for a long time, and there is going to be a gradual deterioration in the value of the dollar. You see it in the stock market. You see it in our own industry. So we feel, or frankly I feel—I will speak for myself—the fact that the price indexes are flat does not cut any ice with me. The way people are fleeing from fixed income obligations into equities is the important thing.

Representative PATMAN. It is the psychological part.

Mr. O'LEARY. Yes, sir.

Representative PATMAN. That is where you come in an adverse way. When you were putting out these ads in the beginning of 1959, alarming the people—and it did alarm them—about inflation, they began to think, these big life insurance companies say we are going to have inflation. We have to watch out. We better begin to look at our personal situation.

Mr. O'LEARY. This is a case of which came first, the chicken or the egg. Somewhere you have to step in and start warning people about inflation because you will never have the opportunity when you don't.

Representative PATMAN. When inflation actually exists, it would be a public service but when you begin to warn about inflation when it does not exist, you are scaring them to do what you complain about, Mr. O'Leary, I am afraid. In other words, they say why should we stay on a fixed income. Why not go into the stock market or go where we can have an appreciation of values.

Mr. CONKLIN. We are not saying that inflation will take place. I think we are acquainting the public with the dangers of inflation and attempting to get their support for measures which would restrain inflation. One of the reasons that the price level has been relatively constant in the past 12 months has been some of the measures taken to correct the fiscal situation. One very important thing, I think, has been the conversion of a substantial Government deficit into the prospect of a balanced budget. This has been of great help both psychologically and actually. The monetary policy of the Federal Reserve has likewise been of great help.

Representative PATMAN. One of the best ways to fight inflation is to cause people to pay their debts. But if everybody paid their debts, we would not have any money because our capital system is based on debts. I just wonder if you often get expansion and inflation confused. I am quite sure advertisements I have seen do not sufficiently distinguish between a needed expansion and growth in our country and inflation. The type of advertising that I have seen would indicate that any expansion, any increase in prices, would be inflationary. Don't you think that these advertisements should be careful to point out that there is a difference between economic growth and inflation?

Mr. PATRICK. Mr. Patman, I don't know what actually was in the minds of those who determined this advertising program, but certainly we all know that there are many very able and very distinguished people who are advocating inflation as a way of life. Consequently, I think probably in the minds of our people was the need to do something

to counteract or neutralize that kind of approach to things because we don't believe in it. We do believe in growth and healthy growth is obviously something this country has to have. We who are administering savings are making a great contribution to the growth process.

Representative PATMAN. I know you are.

Mr. PATRICK. We are trying to do it very intelligently. I don't know whether we always accomplish it or not.

Representative PATMAN. I don't know anyone in Congress who is advocating inflation. A lot of Members are branded inflationists and are accused of wanting to spend our country into prosperity but when you know those Members you will find it quite different.

Mr. PATRICK. I am sure this was not specifically directed to Congress.

Representative PATMAN. You are talking about some of the economists who have testified before our committee.

Mr. PATRICK. That is right, and articles in very sophisticated journals, advocating that a little bit of inflation is a way of life and should be embraced as public policy. We don't believe in it.

Representative PATMAN. I don't advocate inflation, but I advocate expansion and growth. I think the countries we have been helping abroad have been expanding greatly while ours is not expanding nearly that much. I think we have been discriminating against our own people in this foreign aid program. That is different. I would like to see Congress stay in session every year in good times or when times are not bad until the budget is balanced. I think the national debt is almost immoral to this extent. I think it is in competition with the progress of the country. We have to have so much debt to have so much money and when we have this huge national debt, that restrains other people. If we could reduce this national debt other people could go into debt and we would not have inflation. I look upon our national debt as something that we should seriously consider every day of our lives and reduce it as soon as possible. I am sure we will not eliminate it.

Mr. O'LEARY. You will not get any argument from us on that.

The CHAIRMAN. Congressman Coffin.

Representative COFFIN. Thank you, Mr. Chairman.

While we have you four financial managers of insurance companies here, I would like to have you address yourself to this question. What happens, what do you do in terms of your portfolios, when we go from a condition of fairly easy money to a condition of fairly tight money with higher interest rates? What happens to you people on the firing line? What is the effect on various sectors of the economy, on State and local governments, on housing, on small as opposed to big business? Can you tell us from your own experience how your portfolios change when these changes occur?

Mr. CONKLIN. I think we all have ideas on that. Mr. Paynter, of the New York Life, might want to comment.

Mr. PAYNTER. We find a definite effect on the total amount of money we have available to invest when money becomes tight. This is because a life insurance company has a number of demand obligations, moneys which are left with us by proceeds of policies but may be withdrawn on demand and our policy loans and dividends left on deposit. When money becomes tighter those moneys which have been left on deposit with us tend to flow out. Fewer amounts of that type

of demand deposits are left with us. We have a very considerable shift. I know that between 1956 and 1957 in that kind of money, we had a reduction of about 20 percent because of that operation, of the amount of money that we had to invest.

Representative COFFIN. What percentage of your money is this demand money?

Mr. PAYNTER. That is left on deposit with us?

Representative COFFIN. Yes, roughly, how large is it? Are we talking about 5 percent or 15 percent or 25 percent?

Mr. PAYNTER. It is hard to express it that way.

Mr. CONKLIN. It is best to express it as a percentage of the cash flow.

Mr. PAYNTER. As I say, the change caused a reduction of 20 percent in our cash flow other than repayments. That, of course, is only part of our cash flow. Also we have payoffs on our mortgages which are a very important element of cash flow to us. Historically when things are running along smoothly, about half of the repayments that we get on mortgages are contractual repayments. The monthly payment with which we are all familiar. The other half we receive are voluntary repayments. Voluntary repayments in a period of tight money are sharply curtailed. I would say that we have experienced as much as a 50-percent or 60-percent contraction in our voluntary payment. A fellow is not going to pay a 4-percent mortgage and borrow some place else at 5. In a period of easy money, he is always trying to refinance his mortgage. We very definitely feel in the amount of money which we have available to invest, the difference between tight money and easy money.

Representative COFFIN. Is there any change in the portfolio with respect to the securities you hold?

Mr. PAYNTER. No. We simply buy fewer of the available securities which are attractive at the time. For instance, in the field of housing, which I am sure we are all interested in, we still put approximately the same percentage in housing of what is available.

Representative COFFIN. I would have thought there would be a decline in your loans to mortgages.

Mr. PAYNTER. There is an absolute decline, but of the percentage that is available, they get the same.

Mr. CONKLIN. I would say that at any given time life insurance funds, as any funds of trusteeship of individuals, would tend to flow into those areas which offered the most attractive returns for those policyholders, considering the risk. Consequently, in a period of tight money you would not change the nature of your operation at all in this respect. Those forces would still govern. But you would certainly direct your money away from interest rates that were fixed and lagged behind and were not fully competitive with other investment outlets. For example, we would definitely put less of our funds in any fixed interest rate commitment, such as FHA mortgages. If the rate were fixed and it were completely unattractive relative to what we could do elsewhere we would cut the funds that we would put there. This is a very natural procedure. The reverse would be true on the other side.

Representative COFFIN. Mr. O'Leary, do you have any comments? I did not include you in my question. I wanted to get the people who

were actually in charge of making decisions to express their opinion.

Mr. O'LEARY. I would like to have Mr. Badger try his hand at this, but there is one point of clarification. It seems to me it will be helpful to note that on an FHA mortgage, or VA mortgage, where the contract rate of interest has a ceiling on it—where, for example, the rate cannot be any higher than $5\frac{1}{4}$ percent—it is possible to buy these mortgages at discounts. You might say, Why don't the insurance companies buy $5\frac{1}{4}$ percent VA mortgages at 96 or 95? Why don't they equate investment yields through the discount mechanism? I think this is an important consideration because a lot of people can't understand why anyone would say, for example, that the life companies might shift somewhat away from FHA or VA mortgages because of the fixed rate.

Traditionally the life insurance companies, I would say, or a very large part of them, have been exceedingly reluctant to buy GI mortgages, in particular, because that is where this phenomenon occurs, at a discount. The reason is that early in the history of the VA program it was quite clear in the law that the veteran was entitled to a 4-percent loan. The lending institutions felt if they bought the mortgages at a discount somebody was paying that discount and it was likely to be the veteran. They felt that this smacked of illegality somewhere along the line. So the life insurance companies have never been discount buyers except that they might buy at a couple of points discount, particularly since the law was changed 3 or 4 years ago, that made it clear that discounts were legal on these VA mortgages if the seller of the house paid the discount. I know in talking about this question with a lot of people there has been confusion. The fact is that the discount mechanism does not work in the case of FHA and VA mortgages. The rate itself has got to have more flexibility in a period in which interest rates are moving generally and other competitive rates are moving.

Representative COFFIN. As a current observation, are FHA's available now? Is the interest rate high enough so that there is active business in this field?

Mr. O'LEARY. In the case of FHA, as we said in our statement, there is an average market prevailing price on FHA's of somewhere around 96. In the case of FHA, I think at the present time most insurance companies would be willing to buy FHA at 96 and a little lower and feel they were attractive. At this particular time, I think there is still a good flow of FHA funds at that particular price.

Mr. CONKLIN. I personally think the flow is going in the wrong direction. They are becoming relatively less attractive.

Mr. BADGER. I would like to emphasize this cash flow, because that is very important to us. To give you a specific example, money began to get very tight in 1956 and 1957. One of the phenomena that many of us observed was that our net outflow of loans to policyholders, which is a demand obligation over which we have no control, began to go up very rapidly. In my company we had been averaging a net outflow—that is new loans versus repayments—of about a half million a month consistently for the past few years. It began to rise to about a million dollars a month and then a million and a half dollars a month. Here was a trend going on and you began to say to yourself something is happening here. If you lend more money

to your policyholders, you obviously are not going to have it to lend to meet other commitments. So the natural effect in our own company was this. We said maybe we won't have anywhere near as much money to invest. We better cut down on the forward commitments we are making because it would be terrible if we could not meet them. So it does have a very practical effect. The same thing is beginning to happen now; whether it is an interest rate phenomenon or what, I don't know. It has very pronounced effects. A period of tight interest rates such as we are experiencing now also has a very profound effect on your day-to-day investment policy decisions.

For example, under competitive bidding the SEC has ruled that it will not allow a public utility to issue a bond where the buyer is protected against having it refunded at a lower rate sometime in the future. Consequently, it may look very attractive now to buy a 5 percent public utility bond, but knowing that we are in a managed money situation, you also know that probably sometime in the next 10 years they could refinance that 5 percent bond at $3\frac{1}{2}$ or 4 percent. So the bond therefore is not attractive to us as a long-term investor. We in our company therefore, buy almost no public utility bonds. We are concentrating on trying to buy things where we can protect our portfolio at present high rates over a long period of time.

Mr. PATRICK. I was merely going to join with these men in saying that one of the principal effects of tight money on us is that it reduces our money flow for the reasons that have been given. Consequently, we have not as much money to invest. The other thing that it does is this: To the extent that any of us desire to shift any of our portfolio from one type of asset to another, it tends to freeze us in the portfolio that we hold because of our unwillingness and many times our inability, to take the losses involved in selling a security and putting the proceeds into another security. Apparently in our company we don't quite do what these other gentlemen say to do with respect to quoting discounts on mortgages. We are perfectly willing to put an offer in the market as long as it is legal to do so at a price which produces a rate that is suitable to us. However, the actual decision does not rest with us as a lender. It usually rests with the borrower. When we had VA rates at $4\frac{3}{4}$ percent, we were quoting a discount 2 to $2\frac{1}{2}$ points greater than we were on FHA. That was a pretty deep discount. As a result it was generally impossible for a broker or builder to get together with the borrower and work out a deal with that much discount involved. Consequently there was not much VA loan business being done. So in effect the low fixed rate on VA loans restricted very severely the flow of money into that particular market, even though some lenders were perfectly willing to quote a price at which they would do business on a $4\frac{3}{4}$ rate.

Representative COFFIN. Thank you all for your contribution.

The CHAIRMAN. Senator Javits.

Senator JAVITS. I am sorry I was not here at the beginning of this questioning on the statement, but I have gone through the statement, and I find two things which are of very burning interest to me. One is your recommendations for an enhanced program of the sale of savings bonds. This is a matter which I have given considerable attention to and in respect of which I have been in communication with

the Secretary of the Treasury and with the President, because it is my deep conviction that at a time like this, when we are very much at war—though a cold war—it is out of the question that we do not make the same effort to sell our debt to the public when we are in a hot war. When you are spending \$40 billion a year for defense, I cannot see how you can conceivably refrain from a massive effort to sell the public the debt. You can't call them war bonds. You certainly can call them peace bonds, because that is what they are.

To what extent do you feel that if we did this—as I understand it, only 15 percent of the public debt is held by the individual saver or investor—would we have an effect on the inflationary fear which to my mind is the great fear which is driving up interest rates? Unhappily, notwithstanding the testimony of all the wise men, I think it is far more psychological than economic. Would you be good enough to comment on that?

Mr. CONKLIN. I would give you my views on that, Senator. I think it is absolutely vital to make the savings bond program attractive. This is merely to restore its relative attractiveness compared to other savings media to the extent that it was there 5, 10, 15 years ago. Its relative attractiveness has been allowed to decrease, so that today the savings bond is completely unattractive. Therefore, it cries out to be made more attractive.

I think that the market for small savings bonds on the part of small individual savers is the greatest single potential market for the sale of long-term Government bonds, provided they are made attractive to these individuals. I think that this would have a very definite anti-inflationary effect in enabling the Government to put its bonded debt into the hands of real savers.

Mr. BADGER. Could I speak to that, Senator?

Senator JAVITS. Will the new 3.75-interest rate ceiling the administration is seeking on savings bonds put them in line with the previous pattern of relationships to other forms of savings, or is that too low?

Mr. CONKLIN. I think it is too low.

Senator JAVITS. What do you recommend as a figure?

Mr. CONKLIN. I would hesitate to recommend a definite figure. I would say you can go back and calculate relatively what the precise figure would be compared to savings and loan deposits, savings deposits, long-term Government bonds, and corporate bonds. It would require a higher rate than $3\frac{3}{4}$. I would say in the small saving area it would need to be somewhere in the area of 4 percent. This is just an offhand judgment. We have given you a table in the testimony, table 12, which gives you specifically the rates of return on the savings bond program and relates them to other savings media in several years. For example, in 1941, 1945, 1948, and 1952. It can be readily seen that the series E program, as well as the others, has declined in relative attractiveness. Back in 1941 I don't think there would be anyone who would question that for the small saver there was no place that was as attractive to put his money as in Government savings bonds. I think at the present time, candidly speaking, there would be no place that would be as unattractive to put his money as in savings bonds.

Senator JAVITS. Based upon these figures and your analysis, as I see it, there is a reference to a difference of about 150 percentage points, which would mean that you would bring your rate up nearer to 5 percent than it is at the present. Nearer to 5 than to 4.

Mr. BADGER. Mr. Javits, may I speak of that for a moment?

Senator JAVITS. Surely.

Mr. BADGER. I am in thorough agreement with what you said. I will go farther. It seems to me that the most important currency in the world today is the dollar. It must be preserved at all costs. The most important debt and credit in the world is the debt of the U.S. Government. Anything we can do to recast this debt so that it is not inflationary in character and not be concentrated as it is increasingly being concentrated in the commercial bank short-term area is worth doing regardless of the price. We have made certain recommendations which we think should be pursued. One of them is rate. Whether it is 5 percent or $4\frac{1}{2}$ or 4 is immaterial to me. Sell the bonds to the people.

No. 2, we have suggested exploring paying commissions to the most marvelous distributing organization in the world, which is our security distributing organization. If it costs some money to do it, nevertheless, the task to be done is of vital importance.

Third, we have suggested, and I know it is abhorrent to many people, that maybe you could give some sort of tax exemption to a limited amount to people who buy savings bonds and hold them. I do not say these things should be done. I say everything should be explored because this is the most important job I think we are facing.

Senator JAVITS. Is there any part of the Federal debt which has tax exemption?

Mr. BADGER. I think there is one partially tax exempt still out, which is a very small issue.

Senator JAVITS. In other words, the whole Government policy has been against it.

Mr. BADGER. Yes, sir. We are merely suggesting the exploration and consideration on a limited basis for savings bonds which I believe they have done in England with small bonds, with considerable success.

Senator JAVITS. Would you take the interest ceiling off savings bonds if you are going to take it off the other market?

Mr. BADGER. I would personally.

Senator JAVITS. What is the view of the panel?

Mr. O'LEARY. May I interject at this point, I believe the bill does provide for taking the interest ceiling off savings bonds and I think the 3.75-percent rate is merely what the Treasury feels that they would offer at this particular time. I think that the ceiling is to come off. This is their best judgment as to how high they would be willing to go at this time.

Senator JAVITS. You think they are low?

Mr. O'LEARY. I think that all of this group would feel that 3.75 is still too low. One thing that is important to keep in mind, however, is that in the case of these savings bonds they are demand obligations. You can get your money back at any time. In the case of a marketable bond you do run a risk of a price loss if you sell in a period of high interest rates after the price has fallen. So that the saving bond is a different sort of animal from the marketable Government bond or from any corporate bond. It has certain qualities about it that I think would tend to make it more salable; 3.75 is the Treasury's estimate of where they could sell at an increased volume. It is a matter of

judgment. Our judgment would be that 3.75 is not quite high enough. I think the bill provides for the ceiling to be taken off and this is their best judgment of how high they think they need to go in order to restore the competitive forces.

Mr. CONKLIN. My feeling is that this is an area where there are substantial numbers of savers willing to purchase savings bonds and all we need to do is to make it attractive for the small individual to save in this area. I don't think we should shop around and say whether it is 3.75 or $3\frac{7}{8}$; let us make it attractive. Previously they were outstandingly attractive. Let us make them attractive again.

Senator JAVITS. Do you have any desirable ratio which the savings bond holdings ought to have to total debt which is bonded?

Mr. CONKLIN. No, I would not.

Senator JAVITS. Right now it is 15 percent. Would you set any objective for the United States?

Mr. CONKLIN. I think I would recognize Dr. O'Leary's distinction between a demand obligation. Nevertheless, you can make the same point about the demand obligation of a mutual savings bank or a savings and loan association. But look what has happened to them over the recent years. They have constantly increased and there has been no decrease. With the growth in our country, we could without doubt sell a great deal more in this area.

Senator JAVITS. Finally, I would like to ask you about this question of price stabilization. I notice you come out very strongly against open market purchasing as well as price pegging. You also come out against buying long terms in order to increase the amount of reserves rather than reducing reserve requirements. Is there any way that you can see that the Government, the greatest debt seller in the United States, can do what any banking firm would do when it put out an issue?

Could it do something about the stabilization of the price of that issue, even for a reasonable period of time? Most Wall Street firms will give some protection. They are not going to buy them all the way up. They are not going to buy the whole issue. They have only a limited commitment. They would give some protection for a year and sometimes 2 years—generally a year. Is there any analogy? I see you come out flatly against all of that.

Mr. CONKLIN. Yes.

Senator JAVITS. Is there any analogy between what the ordinary banking firm does to protect the ordinary issue and what the Federal Government can do within your view feasibly from the public policy and economic point of view?

Mr. CONKLIN. No; I think there is a very substantial difference between the corporate support operations to the extent that they take place, which I think is a very minor extent, and the Government. The corporation may be borrowing once in 5 years or 10 years and has one or a few issues outstanding. The Government is in there all the time with one big issue after another. You would be continuously supporting the market for all issues and be back to a pegging operation. This is what we vigorously oppose.

Mr. O'LEARY. On that point another very important distinction is that any support of a particular corporate issue is done with means that don't involve the ability to create credit. When the Federal

Reserve supports it they have the unique power to create credit in the process. That is a very important distinction.

Mr. BADGER. There is one more distinction on that, too, Senator. You speak of the support that is given in a private issue when it is floated in Wall Street, that is confined to a given issue. If the Federal Reserve should attempt to do the same thing in governments, it would not be supporting just that particular issue. It would be supporting the whole outstanding debt structure because they are all interdependent.

Senator JAVITS. That was my question. My question was, suppose that the Government puts out a new issue of long-term bonds, would you countenance support of that particular issue for any length of time analogous to what a corporation would do for some limited time?

Mr. BADGER. I question whether it would work. Certainly in a rising interest-rate market it would not work. If it happened that the specific issue being sold by the Government was slightly overpriced, it would not work.

Senator JAVITS. Assuming that is the answer of the panel, may I ask this: Would you in any way relate inducements to sell savings bonds to the need for stabilization of a long-term market? In other words, would you increase those inducements by increasing the interest rate or any other conditions which would alleviate some of the pressure for floating debt through the sale of savings bonds? Would you relate those two operations?

Mr. BADGER. I am not quite sure I know what you mean.

Senator JAVITS. At a time like this, would you give a higher interest rate and greater inducements to the savings bond buyer than you might normally? The Treasury is giving us a figure of 3.75. They think that is enough. Maybe that is not enough because if they are not going to do anything else about getting this debt put in to more secure hands and if they cannot float long-term bond issues with others, the thing is to offer greater inducements to the savings bond buyer who can soak up \$20, \$30, \$40 billion of open debt which you cannot sell in the open market at long term to date if you don't want to engage in a pegging operation except at ruinous interest rates.

Mr. BADGER. I think I said earlier that as far as savings bonds were concerned, I would offer whatever is necessary to do the job because I think it is essential to be done.

Senator JAVITS. What is the job?

Mr. BADGER. To sell as many as you can.

Senator JAVITS. As many as you can without regard to how many?

Mr. BADGER. I think you are within practical limitations of what could be sold anyway. You know what the savings flow is.

Mr. O'LEARY. I think this group—and our statement bears it out—feels that as events have transpired in the last 10 or 15 years, perhaps the primary market for the U.S. Treasury today for long-term bonds is individuals. Small individuals. We would, I think, feel—at least I feel this way myself—that it would not be disturbing at all if the proportion of long-term marketable debt declined if that could be offset with an increase in savings bonds outstanding. In other words, if we get the debt in the long-term form, within practical considerations, I don't see that it makes an awful lot of difference whether we do it by increasing the savings bonds or by selling marketable bonds.

We feel that the natural market for long-term Government securities is in the hands of individuals and the savings bond is the type of vehicle we have used, so let us push that and sell as many as we can.

We think it is going to be hard to sell them because we think it is hard to sell fixed income obligations of any kind in a period in which the general public has become alarmed about inflation. But let us accelerate that as much as we can. Let us sell them there. If it turns out that there are a lot of long-term savings bonds outstanding and the proportion of marketable bonds is much lower, that will not disturb us.

One other thing I think you should realize is that we all appreciate that to the extent that savings bonds are sold it is going to be competitive with life insurance and other forms of savings. We all feel, however, that it is vitally important that the U.S. Government finance itself soundly. That is the basic thing.

Senator JAVITS. That has a correlation to your opposition to pegging or other open-market operations by Government agencies in Government bonds; is that correct?

Mr. O'LEARY. Very definitely.

Senator JAVITS. Thank you.

The CHAIRMAN. It is always valuable for members of the financial community and Members of Congress to indulge in mutual criticism. Members of my community are accustomed to long-distant criticism from the financial community. We also welcome close-range criticism. I hope you gentlemen will not object if we make this process somewhat reciprocal. I may say that many of us had our feelings hurt by this newspaper campaign on inflation which you people launched in January, February, and March. It came almost immediately after the Republican National Committee announced that inflation was to be an issue in the 1960 campaign. It was accompanied by a similar campaign against inflation in the more partisan Republican newspapers of the country. It seemed to be part of a general political campaign pointing to the 1960 elections. To many of us it seemed unjust in view of the fact that it came, as Congressman Patman said, when prices were stable and at least have continued stable to the present.

Now I want to make some comments about this, if I may.

In the first place, I assume that the cost of these advertisements, which certainly must have run into millions of dollars in the newspapers of the country, could be deducted as a business expense. That I assume is correct.

Mr. O'LEARY. The expenses of that advertising program are defrayed by the Institute of Life Insurance, which is a trade association, and is financed by contributions by life insurance companies.

The CHAIRMAN. So that ultimately they were deducted as a business expense by the member companies. Some of these were direct advertisements of companies.

Mr. O'LEARY. Senator Douglas, let me say this: I feel a little bit ill at ease answering this question because there are none of us here who are connected with the Institute of Life Insurance. I think we might proceed by saying it would be my assumption that you are right on that. I would like to talk with the president of the institute and perhaps maybe we can submit a statement.

The CHAIRMAN. Many of these ads were inserted by individual companies as well as by the life insurance institute?

Mr. O'LEARY. Yes.

The CHAIRMAN. I take it the cost, whether directly or indirectly, was charged off as a business expense. When it is charged as a business expense this decreases Government revenues.

Mr. PAYNTER. I beg your pardon, sir. I don't think that would be deduction against investment expense, which is the only expense which we can take in determining our taxes. At least in my company, advertising is not charged as an investment expense. We can only use investment expenses against income under the new law.

The CHAIRMAN. Certainly, under the old law you could not deduct it.

You can take ordinary administrative expense.

Mr. PAYNTER. Not unless it is directly assignable; and we have not considered advertising as assignable as an investment expense.

The CHAIRMAN. This is something new in the business world. I always assumed that advertising was a business expense and therefore diminished the revenue.

Mr. PAYNTER. The Bureau of Internal Revenue has been very sharp in what it has been willing to let you charge.

The CHAIRMAN. I wonder if the staff will explore this. My own judgment is that it is a business expense. I am advised that it is a business expense.

Mr. PATRICK. I am not familiar with deductible expenses under the new tax law. It was not a deductible expense under the old law.

The CHAIRMAN. This campaign was conducted prior to the passage of the new tax law. I will comment upon this in just a minute. Indeed, it was conducted at the same time when in the Senate Finance Committee, of which I happen to be a member, we were considering the new tax law. My point is that if it were deducted as a business expense, and I believe in a large proportion of cases it was, the Federal Government paid a considerable portion of this cost in diminished revenues. Therefore, this resulted in an increased Government deficit. And increased Government deficit would require increased borrowings by the Government. So that this campaign against inflation contributed to inflation. That is my first comment.

My second comment is that it pained some of us to have this campaign conducted at a time when the insurance industry—I won't say the life insurance industry—was fighting any increase in taxes. Previously, the insurance industry paid 52 percent of 15 percent of net income, or 7.8 percent on profits, with no taxes on underwriting profits. I think my earlier statement is correct, that it was not bearing its fair share of the load. I happen to have been a member of the Senate Finance Committee as we were considering these bills and there were hundreds—I think there were two or three hundred representatives of the insurance industry—who came into the hearing room and protested against the bill which came over to us from the House. We all are somewhat inconsistent in life. I know that. Politicians are sometimes inconsistent. But we are not the only people who are inconsistent.

It really pained me to see the life insurance industry which, on the one hand was saying we must balance the budget, and so forth; and on the other hand resisting to death, almost, any increase in taxes which would have helped us to balance the budget.

As I say, mutual criticism is good for the soul and we politicians are on the receiving end nearly always—and I thought you would not object if for a brief moment we reversed the roles.

Mr. PATRICK. Is it not any different from what you encounter from other businesses?

The CHAIRMAN. I had hoped more from the insurance industry.

Mr. CONKLIN. I do not think there is any inconsistency in the position of the life insurance industry on taxes. I think that the huge increase in insurance taxes, which are a tax on the small savers of the country, was quite ill advised when we are fighting inflation. I think some stimulus to savings is exceptionally important in fighting inflation. At a time, therefore, when you are trying to fight inflation, it is highly inconsistent when you take measures to increase taxes on the small savers. Thus, I think there was no inconsistency about this position as far as I was concerned. The inconsistency, in my opinion is just the opposite to your assertion, Senator.

Mr. O'LEARY. Senator Douglas, there are two comments I would like to make. One is that at least I have inferred, or I think you suggested, that this most recent campaign of the institute was timed at a particular time to coincide with part of a broad campaign.

The CHAIRMAN. I did not say this. I said it was coincidental. It was so coincidental as to raise very interesting questions in our mind, particularly when it was accompanied by this newspaper campaign. You say it was perchance.

Mr. O'LEARY. I would like to allay your fear. It was perchance. As you well know, it takes quite a time to prepare a campaign of this sort. When you get involved in the advertising business, it is a time-consuming process to get all these copies. It is pure coincidence that it came at that time.

The CHAIRMAN. Does it take time from the 15th of November to the middle of January?

Mr. O'LEARY. That is No. 1. No. 2 is this: You suggested that the life insurance business came down here and fought—

The CHAIRMAN. Perhaps I should say the insurance business. Perhaps that is a better description, because the stock companies were a much more favored group than mutuals. I want to make an exception in the case of mutuals.

Mr. O'LEARY. There are lots of people who can discuss this question of what the insurance industry did or did not do in this. I think one of the criticisms in the industry is really the fact that what the insurance business did was pretty much accept the idea that they are going to pay more taxes and the fight was how do you distribute it fairly among the companies, so you don't create inequity. I don't think the insurance industry ever made any great fight against increases in their taxes. The big fight was in terms of how do you do it equitably.

The CHAIRMAN. I am very glad to be reassured on this point because I listened to great many days of testimony and everyone was opposed to an increase in taxes on their particular branch of business. Their thoughts in the back of their mind might be different. As I say, I think the stock companies have been much greater sinners in this whole business than the mutuals. There was a terrific loophole in the previous law in not taxing underwriting profits.

Mr. CONKLIN. Senator Douglas, may I make a comment on your general statement of coincidence? I would like to say that inflation is not a political issue. It is a national issue, of crucial importance to the country, and cuts across party lines.

The CHAIRMAN. It was made such by the Republican National Committee.

Mr. CONKLIN. The second thing I would like to say is that the life insurance industry and financial fraternity generally looked with great admiration upon, for example, your fight in 1951 in the fight against pegging Government bonds. I think it was a statesmanlike thing, and I think it drew the nonpartisan admiration of the financial fraternity, as well as elsewhere.

The CHAIRMAN. When a Democrat takes issue with a Democratic administration, he becomes very popular in financial circles and that happened to be such an occasion.

Congressman Patman has to leave.

Representative PATMAN. I have to be on the floor soon.

I wonder if I may submit some questions to these gentlemen with the understanding that they will answer them for the record if I get them to them before they inspect the record. Will that be satisfactory, gentlemen?

Mr. O'LEARY. Certainly.

The CHAIRMAN. Senator Bush?

Senator BUSH. Thank you, Mr. Chairman.

I am sorry, gentlemen, that I was not here to listen to all of your testimony. Unfortunately we have hearings going on in the Banking and Currency Committee on the housing situation. Both the distinguished chairman and I are supposed to be in two places at once. I usually try to be where he is so I can hear what he has to say. But this morning I was not able to do that. I understand that the chairman was somewhat critical of the representatives of the insurance companies for having spent some funds in alerting the public to the dangers of inflation. Is that so?

The CHAIRMAN. I made three points. First, that it occurred at the same time that the Republican National Committee announced that inflation was going to be a great issue for 1960. I have been assured this was purely coincidental. The second that it was undoubtedly in many cases charged off as a business expense and hence diminished Government revenues to that extent, and hence increased the deficit and contributed in some degree to the inflation which the advertisements decried.

Senator BUSH. That would be true of any form of advertising, would it not?

The CHAIRMAN. Yes. This is a peculiar type of advertising.

Senator BUSH. Peculiar because the Senator does not like it, perhaps.

The CHAIRMAN. No. It is designed to influence political decisions.

Senator BUSH. I hope it will have some influence.

The CHAIRMAN. This industry was ostensibly engaged against inflation but in some effect contributed to it.

Senator BUSH. I thank the chairman for giving me his views.

The CHAIRMAN. I had another point.

Senator BUSH. You have given me enough. What I wanted to say was that I have noted with great interest and approval the advertising campaign that was developed by the industry and I think it has been long overdue. I was surprised that 20 years ago the insurance industry was not alerting the country to the dangers of inflation at that time because I think it has a very direct bearing on their business and on the security of the savings of the people that are represented by the millions and millions of policies that are outstanding. I can't think of any more useful way that the insurance companies could advertise than in an effort to protect the very values that they are trying to sell to the people and protect the savings of the people that are entrusted to them. I could not disagree more strongly with my good friend from Illinois on anything than I do on this particular matter.

I don't believe that any industry who happens to voice firmly held beliefs and very deliberately arrived at conclusions concerning very important matters of national policy should be abused or reprimanded—I will withdraw the word abuse—

The CHAIRMAN. May I ask these gentlemen if they felt that I was reprimanding them. I said I was very glad to see their criticism which generally members of my party receive at long range and we are delighted to have them criticize us at short range, but I asked if they would object if we made this process mutual and if I ventured to criticize and express my reservations on this point. If these gentlemen feel I treated them unfairly, I want to assure them it is not my purpose to do so.

Senator BUSH. They would be a little frightened to confess.

The CHAIRMAN. No. These people are financial giants, and are not intimidated by financial pygmies.

Senator BUSH. I thank the chairman for what he said. I understood from what he said he was critical of the fact that this might be charged as a business expense. I assume he disapproved of it or he would not have mentioned it.

The CHAIRMAN. I thought it contributed in some measure to the inflation which they decried publicly.

Senator BUSH. I simply make the point that I believe in a business like their business where they are the trustees for so many millions of families' savings that it is incumbent upon them to do what they can do to influence public and political opinion, if necessary, in the interest of preserving the value of these assets which are entrusted to them. I just wanted to make that point very clear.

Now I will yield to this gentleman.

Mr. PATRICK. I merely wanted to comment on something I said previously. I think it is easy in a discussion of an issue such as this, to get the part that we as savings institutions play completely out of context. We had no political intention one way or another with respect to this. I mentioned it to Senator Douglas and I will repeat to you, Senator Bush, that there is much being written and spoken today by some very knowledgeable and sophisticated people in this country that inflation is a desirable thing. It is a way of life.

As a matter of fact, we feel that is exceedingly detrimental to society and to the business we are engaged in and believe in. Consequently, we feel perfectly justified in spending some money to coun-

teract that. It is not directed toward Congress. It is not directed toward any political party at all. It is purely and simply in the realm of ideology as to what is a proper way of life. We may be wrong but we are at least convinced.

Senator BUSH. I hope some of it will filter through to the Congress anyway even though you didn't direct it that way.

I have no further questions.

The CHAIRMAN. Congressman Coffin.

Representative COFFIN. I would like to ask a question that bears on the subject matter that Senator Javits was talking about, this matter of increasing the salability of the series E bonds or bonds of that nature.

What would be your thinking with regard to this approach, if the Government made the series E bond a permanent bond which would carry interest, with no termination date on the bond? The interest would be declared periodically in accordance with the realities of the market. The restriction on the bond would be that it could only be held by individuals. This would recognize in a very concrete way that we thought this was a primary home for a long-term debt and would place the individual in a much more permanent position than he is now. This would be the objective. What do you think of that approach to the people's bond?

Mr. BADGER. I would say, sir, that I think it ought to be explored. I don't think any one of us here is ready to say we think this is a wonderful idea. I think everything should be explored.

Representative COFFIN. You think it is at least worthy of exploration.

Mr. BADGER. I think everything is worthy of exploration.

Mr. O'LEARY. Just so we are sure what you are talking about, this would be a perpetual bond where the interest rate might start off at 3.75, and if on the basis of some criterion it was decided it should be for 2 years hence, automatically it would be raised to four, and 5 years hence if it came down to three it would come down to three. In other words, the interest rate would be kept in tune by some particular criterion so that there would be a variable interest rate made flexible in the light of market conditions. This is the sort of thing you have in mind?

Representative COFFIN. Yes.

Mr. CONKLIN. I would agree with Mr. Badger that any idea of this type should be explored. However, a bond not having a maturity presents difficult problems because the individual saver may want to have a definite maturity date at which he can realize upon his principal with no sacrifice in yield or principal. If you put it in the form of a permanent bond and you wanted to discourage early cashing in, you could not give him par for it, so you would have to have a discount and this might hurt its attraction.

Our only point would be that they should be made attractive as instruments specifically designed to attract the small saver. If this one thing that you suggest would do that, then I think it would be worthwhile. I think it should be investigated, although I have serious reservations.

Representative COFFIN. Within your industry, have you explored this particular suggestion?

Mr. CONKLIN. No. I would say that we have felt that the savings bond instrument as designed originally and priced with relation to other competitive outlets was a very attractive instrument. It may be improved. What remains to be done is to restore it to its former attractiveness. This is the predominant consideration we had in mind.

Representative COFFIN. I like very much your suggestion for a deferred payment for bonds. This relates to other than series E-bonds.

Mr. CONKLIN. Yes. This is for the institutional bond purchaser.

Representative COFFIN. I was wondering whether it would not be sensible to make it possible for the individual to purchase larger bonds than series E-bonds. Would this at all be practical?

Mr. CONKLIN. In my opinion this would not be too practical. I think the bulk of the saving in the savings bond program is handled rather efficiently through the payroll deduction. One of the points of attraction of the savings bond is that you are able to put in a small amount, whereas, if you buy a bond that is \$1,000, there are very few people who have savings of a thousand dollars. I think the average savings of an individual in life insurance is only \$800. The life insurance industry is a mass of small savers.

Representative COFFIN. Mr. O'Leary, do you have a comment?

Mr. O'LEARY. It just occurred to me that if the interest ceiling on savings bonds were taken off and you gave the Secretary of the Treasury some administrative flexibility in determining the rate, aside from the fact that you wouldn't have a perpetual bond, wouldn't you in effect have the same thing there that you would have under your proposal? I think the big thing is that there would be administrative flexibility in the hands of someone and I think you would agree that the Secretary of the Treasury can intelligently exercise that. If the interest ceiling E-bonds were eliminated and the Treasury were given some administrative discretions as to rate changes, perhaps a lot of the benefit of your proposal would be immediately possible.

Representative COFFIN. The only additional merit of this proposal I have suggested, I suppose, is the psychological one of injecting a freshness of approach that has been lost. That is, the series E-bond, like so many good things, when it becomes old, loses the initial feeling that was so important.

Mr. O'LEARY. I think that is a very important point. I agree that this is definitely a proposal that should be explored.

Representative COFFIN. Thank you.

I have one more question which goes to debt management, I suppose. The commercial banks have some competitive advantage over all other financial intermediaries. The question that some of us have been pondering, is whether commercial banks should be required to hold certain amounts of secondary reserves of Government securities?

In other words, a quid pro quo for some of the privileges they have which would by the same token assist the Federal Government in finding a market for some of the securities.

Mr. CONKLIN. Speaking personally, this is a very important question. I don't think we have had a great deal of time to study this. My offhand reaction to it would be very definitely unfavorable. It would be other than relying upon market forces to sell Government bonds which I feel would be completely undesirable.

Representative COFFIN. On the other hand, some of our institutions have certain advantages from the Government. You can't say that some of these advantages have been created solely by the market. They exist by reason of the kind of institution they are and their relationship with the Government. For example, banks in the Reserve System carrying large cash balances interest free have an advantage which is not a product of just economic forces. Are you really distorting or are you correcting when you require a certain quid for the quo that they have?

Mr. BADGER. Don't you almost have that now? The banks by law are required—members of the Federal Reserve System—to have certain reserves which are nonearning assets on deposit with the Fed. Those deposits in turn are now invested in Government securities substantially 100 percent by the Federal Reserve bank. So in effect these idle reserves which the banks are required to carry are invested in short-term Governments as they would be if they were made compulsory secondary reserve. I think the net effect on the Government market probably is not too great.

Representative COFFIN. I think that is all, Mr. Chairman.

The CHAIRMAN. Senator Javits.

Senator JAVITS. Thank you.

The CHAIRMAN. Senator Bush.

Senator BUSH. No, thank you.

The CHAIRMAN. There is only question I want to raise.

Chairman Martin and the Federal Reserve Board are very insistent in maintaining the policy that they would deal in bills only, or almost entirely in bills. The New York Federal Reserve Bank for some years has held a contrary opinion, that the Federal Reserve banks should also purchase longtime securities, of over 5 years duration. A number of eminent economists, including Professor Samuelson of MIT, who is probably one of the ablest of the younger economists, have come to the same conclusion as the New York Federal Reserve.

I wonder if you gentlemen have considered this question as to whether the Reserve should continue its present policy of dealing only in short-term Governments.

Mr. BADGER. I think there are always differences of opinion as to whether the Federal Reserve should restrict itself to short-term securities. That is a matter of controversy, we know. At the present time I think all of us here, because we have discussed it many times, feel that because of conditions as they now exist, with this inflationary psychology, with the beginning of questioning, at least, in foreign quarters as to the dollar, with gold going out, that for the Federal Reserve to be required, or practically be required, or be told it is the intent of Congress, that they do something which could be interpreted—and by most people I believe would be interpreted—as the beginning of a pegging operation, could be most harmful in the spreading of this inflationary psychology.

I think we are at a very, very dangerous juncture here and we can afford to take no chances on this kind of thing. In normal times when you have none of these questions, when the dollar is absolutely unquestioned, which it is not now, sure, I think you can depart from the short-term-only policy. Some of us have disagreed with Mr. Martin on that. I have personally. I think he has shown flexibility and

the Board has shown flexibility, however, in meeting certain situations at various times. I think now to start that kind of operation would be dangerous. I can tell you from personal experience that people abroad are watching what we do like hawks, and I think it would be very dangerous.

The CHAIRMAN. Mr. Conklin referred to the fact that I am the opponent of pegging. I take some credit for it in 1951. It would seem to me that the Reserve could deal in longtime securities, buying long- and selling short-time securities at the same time so that there would be no net increase to member bank reserves.

Second, to the degree that the total money supply is increased—and I think the general view is that it should increase approximately 3 percent a year—that this increase should not take place exclusively in short-time issues but partially in longtime bonds. Whichever method you use increases member bank reserves to the same degree. There is no difference in the amount of ultimate credit which the banks would create, whether you go by the method of bills or bonds. So logically there is no issue of inflation involved in this. I take it what you are saying is that people would be afraid that this would be the prelude to pegging. Not pegging in itself but the prelude to pegging.

Mr. BADGER. I think that is one danger, yes, and that is a personal judgment. This would be an abrupt departure in policy—that we know.

The CHAIRMAN. In other words, you are saying if Mr. Martin had changed his policy 5 years before we would have been all right but since he held out for 5 years he should not do it now?

Mr. BADGER. I think there might have been times that the policy could have been changed but now is not one of them.

The CHAIRMAN. When will it be time?

Mr. BADGER. I don't know. When there is complete full confidence that the United States is going to protect the dollar at any cost.

The CHAIRMAN. You mentioned foreign fears of the security of the dollar. I notice that Chairman Martin mentioned this, after returning from the meeting of the World Bank in New Delhi. I take it the people raising the objections were not central banking authorities of Great Britain and Germany, but included all these other countries. Nearly all these other countries are receiving aid from the United States at the same time they are expressing fear about the financial integrity of the United States.

Senator BUSH. Wouldn't that be logical?

The CHAIRMAN. I was going to say that could we not reassure them and remove these fears by the simple device of reducing foreign aid to these nations, thus increasing our financial stability and contributing to their mental stability so that they would no longer have these fears about us. I would suggest that you gentlemen of the financial world could carry this message to the central authorities of Italy and France and India and so forth, and so on, if they are so solicitous about our financial strength they can take courage. Congress in due time will reduce foreign aid below the amounts requested by the administration and hence contribute to the stability of the dollar about which at presently they are so fearful.

Senator BUSH. Let me ask a question on this same thing. The companies that you represent deposit in the commercial banks. I imagine that those who are responsible for those deposits examine the statements of the commercial banks as to their assets and liabilities to see if they are solvent and liquid and so forth, with particular attention, I should think, to the question of demand deposits and that they would be readily available in the event that they were needed.

Commercial banks do have to be ready to honor demand deposits immediately and they normally, to the extent that they invest, invest in short-term securities. That lends confidence to the banking structure. But if one saw that a commercial bank were investing a large part or any large part of its deposits in long-term obligations, there would be eyebrow raising and questions raised about the way that bank was being managed. The confidence in the bank might be injured.

Do you not agree with that?

Mr. BADGER. Yes.

Mr. O'LEARY. Yes.

Mr. CONKLIN. Yes.

Senator BUSH. The Federal Reserve is the bankers' bank. The same thing is true. The money that is on deposit with them is subject to immediate withdrawal or availability for loans to other banks. Do you not believe, therefore, if they followed a practice themselves by making long-term commitments which they frown upon in connection with the management of commercial banks that this might have a very unfortunate effect on the whole banking system, not only abroad, as you pointed out, but at home? That is the question I raise.

Mr. BADGER. I think so.

Senator BUSH. Is that sound reasoning?

Mr. BADGER. I think it is, sir.

Senator BUSH. It is.

Mr. BADGER. I think so.

Senator JAVITS. Mr. Chairman, may I ask a question?

The CHAIRMAN. Yes, indeed.

Senator JAVITS. Mr. Chairman, I would like to pursue what you raised about some form of open market operation. Suppose the Secretary of the Treasury or the President announced exactly what we were going to do and why, that we have been buying short terms. We are going to give a blending of that operation and buy long as well as short terms as it suits our convenience and our interest. We are determined that somehow or other the course of interest rates upward needs to be reversed in the national interest. We will keep these all within limitations and we are not going to engage in inflation. On the contrary, it is part of our anti-inflationary drive, which is the reason for the tremendous emphasis on the budget and the President's vetoes.

Would that in your opinion avoid the psychological handicap? It seems to me that we cannot, because we haven't got a good public relations technique, fail to engage in some major program essential to the economic stability of the country.

Mr. CONKLIN. Senator, I feel it would have exactly the opposite effect if that statement were made. I think it would make the general financial public that much more worried about the implications, particularly in the connotation you have suggested.

Mr. O'LEARY. May I comment on that, because I think this is an exceedingly important point. Suppose right now at the present time the Federal Reserve did—suppose there was this announcement—begin to buy long bonds to lend stability to the prices of long bonds in an effort to hold interest rates down on Government securities. Senator JAVITS, we are in a period of rising business activity and the demand for capital funds for mortgage financing, for State and local financing, for corporate financing, for consumer credit is all exceedingly great. Even if the Federal Reserve bought long-term Treasury bonds there would be no reason in the world that these other interest rates would not rise. They would tend to go up. What would happen is that insurance companies, savings banks, pension funds, and savings institutions generally, and individuals who hold Government bonds, would see that there would be a favorable opportunity at an artificially high price to sell these Government bonds and to reinvest the money in investments such as mortgages that have gone up in rate. So you cannot have any middleground on this. The minute you start this procedure what will happen is that there will be a big wave of dumping of Government bonds on the Federal Reserve.

What will happen is that if they buy these bonds they are simply going to create all that more public concern about the inflationary situation. At the same time they will have to sell short securities and as they sell short securities and the Treasury is required to sell short securities you will have a sharp increase in the short-term rate. You can get 8 or 9 or 10 percent rate of interest on short-term money in this process. You can have private interest rates go up very sharply and have the Federal Reserve, just as it did in the autumn of 1950, and the spring of 1951, have to buy billions of dollars of these long-term Government bonds to try to hold the thing. It is the market working.

So long as we have a free market economy here and a free capital market, then there is nothing you can do to this situation. You will get bonds dumped on the Federal Reserve if they buy them at an artificial price. There is no middle ground.

Senator JAVITS. Now you are answering Senator Douglas' question differently. I am impressed with your answer now. What you are really saying is that the reason you can buy short terms and not long terms is the difference in market price. Your long terms are now selling in the middle 80s. You take a terrible beating on those and they will give them to you by the bushel. Whereas, your short terms are selling at relative rates at which Government bonds should sell, and hence you don't have the problem. That is the real answer.

Mr. O'LEARY. To a degree.

Senator JAVITS. Not so much the psychology as the practicalities of the situation today.

Mr. O'LEARY. Yes.

Senator JAVITS. If the Government bond markets get in the 95s or hundreds where it ought to be, then your objection would no longer obtain; is that correct?

Mr. O'LEARY. This goes back to what Mr. Badger said. If you have a climate such as early 1958, when there were decreasing demands for capital funds, to have the Federal Reserve step in and buy Government securities at that time would not really cause very much of a ripple. You have to put it in the climate of the situation in which

the demands for credit are rising. You look at the figures that we have in the back of our tables here, and we could give you figures for what has happened in 1959, there is a perfectly enormous demand for capital funds. The mere fact that the Federal Reserve sits around and buys Government bonds is not going to prevent long-term interest rates from going up. The only thing that will happen is that those people who are holding Governments and can sell them at prices that are artificially high because the Fed is supporting that price are simply going to sell them and go into mortgages and other things that have gone up in rate. The thing that is important is that you cannot sin a little on this. They will be in up over their head before they know it. All you have to do is to take a look at the Treasury Bulletin between October 1950 and March 1951 and see the acceleration that occurred there in the selling of long-term Government bonds by all investors. When there is a support price that is artificially high and you can put your money somewhere else, anybody would sell against that artificially high support price. That is what would be bound to happen at this time.

Senator JAVITS. May I ask you another question: I notice that yesterday Mr. Martin brought in some revisions of the productivity index showing that it was rather materially higher than previously advertised, according to his figures. Would that indicate that our rate of adding to the money supply or credit supply is too low? In other words, if we add normally, and what is considered noninflationary, as Senator Douglas has said, 3 or 4 percent a year to the money supply, is this revision in the productivity rate a justification for adding more, also noninflationary, even on a cumulative basis, on the theory that the figures have not been correct for some time now.

Mr. O'LEARY. I would answer that this way: There are other people who can answer that better than I. I feel pretty strongly about this, and I feel it is important that it be understood. I think the one cardinal principle that the Federal Reserve is operating on is the realization that the supply of money in the country has to be related to the size of the economy. In other words, they want to increase the money supply with growth. It has been one of their objectives to do this. I think no one would disagree with me on this. Certainly this group would not. There is a relationship between the amount of money and the size of economy you have. It would be foolish to think you should not increase the money supply as the economy grows. The Fed has been trying to do this. It is a matter of judgment how much you increase it. The thing that makes it difficult is that this is not a smooth, even process. There are cyclical ups and downs. So when you look at that money supply it is difficult to come out with any meaningful relationship because you have these cycles superimposed upon a trend. In their judgment they have increased the money supply with growth. If our rate of growth is faster than we thought it is, I am sure no group would be more anxious to step up the increase in the money supply to have it consistent with growth. I have followed the writings of the Federal Reserve people over a period, and I think one thing that is cardinal in their whole scheme of things is that the money supply has to be related to growth. You may question whether at any particular time, a 2-year period, they have increased it enough, but this is a matter of judgment. My own per-

sonal view is that there is not a better equipped research organization in the world than the staff that the Federal Reserve has.

If any group has economic knowledge and ability to be correct in its judgment, the Federal Reserve has the group to do that. I, for one, would be a lot more confident in their judgment in how much the money supply should be increased with growth than any other group.

Senator JAVITS. Thank you.

The CHAIRMAN. There is just one more question, and then one point to raise with the staff. Let me take the question for the staff to begin with. The issue has arisen as to the degree to which commercial banks or the demand deposits sections of commercial banks invest in long-time Government securities. The Federal Reserve Bulletin for June, page 623, lists investment of commercial banks in 5- to 10-year Government maturities at \$7,591 million. Banks with maturities over 10 years account for \$4,423 million. Or a total of approximately \$12 billion.

Senator Bush makes the very proper point that this may come from time deposits or savings deposits in commercial banks and therefore demand deposits are not so invested.

There is one final question I would like to ask—

Senator BUSH. If the Senator would yield on that point, you have lumped bonds of 5 to 10 years with bonds 10 years and longer.

The CHAIRMAN. They are normally regarded as bonds as distinguished from notes, bills, and certificates which are less than 5 years.

Senator BUSH. That is right as to the title. But maturities of 5 to 10 years cannot be classed in the same asset category with bonds that mature from 10 to 30 years.

As Senator Javits points out, the longer term ones tend to fluctuate in value a lot more than the shorter term bonds. The reason a bank should not be investing demand deposits in longer term issues, longer than 5 to 10 years or 10 or more years, is because they have to write down the market values and if they got into a heavy position in long-term bonds and had to write them off 20 points or thereabouts, which they might today, it would cause not only raising of eyebrows but some withdrawal of accounts.

The CHAIRMAN. Then my friend would not object to the Federal Reserve and the commercial banks investing in bonds of from 5 to 10 years.

Senator BUSH. No; you did not understand me that way. I do not approve, frankly, of the practice of a lot of these banks investing in 5- to 10-year paper.

The CHAIRMAN. I see.

Senator BUSH. Commercial banks.

The CHAIRMAN. My point is that the commercial banks are already investing \$12 billion. It would be interesting to find out whether this comes from reinvestment of demand deposits or the reinvestment of time deposits.

Senator BUSH. I think we should know that.

The CHAIRMAN. This is the final question. We appreciate the courtesy of you gentlemen staying so long. Some of us were distressed by the speculative fluctuations in the Government bond market last year. In the course of the investigations, we discovered at least to

my surprise that there were virtually no required margins in the purchase of these securities. The Chairman of the Federal Reserve Board came up before us in February and said the margins were generally 5 percent. Upon investigation we found that frequently the margins were very much less and in a very large proportion of cases there are no margins at all. We found in the securities dealings in New York that they had an annual turnover rate of their accounts of something like 6,700 percent. That was their turnover rate. This meant that with 250 trading days to a year, a turnover of 25 times in 1 day. This raises the query, Would you favor margin requirements on credit purchases of Government securities?

Mr. CONKLIN. I personally would answer that I think this merits very serious consideration and study. I think the speculation in the Government bond market and sharp gyrations that were caused were a matter of concern to us and most people in the financial community. Steps that might be required to correct the situation I think should be considered. This is an area in which people should have an open mind and consider the suggestion you make.

Mr. BADGER. I don't think any of us has had a chance to read these big volumes. I have just glanced at them. All of us were surprised at the extent of speculation in Governments last year.

The CHAIRMAN. Is it not generally true that no margins are required?

Mr. BADGER. No, that is not generally true. I think what developed was some rather trick devices that nobody knew about. There were no figures about them. It had to do with repurchase agreements.

The CHAIRMAN. The New York Clearing House brought out figures showing an average turnover of the bank accounts of the dealers in securities of 6,700 percent.

Mr. BADGER. That is not surprising.

The CHAIRMAN. The accounts turned over 25 times in a trading day.

Mr. BADGER. That is not surprising, sir. They are probably the largest wholesalers in the world. The transactions that are done are enormous. It is never surprising for large institutions to call up and say we would like to sell 20, 30, or 40 million dollars of bills.

The CHAIRMAN. Twenty-five times in a day is extraordinary. They were doing this business, as I remember, subject to correction, on total accounts—17 dealers had total accounts—of something like \$35 million. They were doing a business in 1 month of \$18 billion.

Mr. BADGER. I don't doubt it. As I say, I have not yet read this Federal Reserve-Treasury study but I think you will probably find if you go to investigate that the heaviest turnover is in bills and things like that where the risks are almost nil and where it is a question of matching orders.

The CHAIRMAN. I know.

Mr. BADGER. I am not an expert because I have never been a Government trader but I think that is the case.

The CHAIRMAN. Do you not think Congress should give scrutiny to this matter?

Mr. BADGER. I certainly think it should.

Mr. PAYNTER. I do, too. I got interested in this last year. As Mr. Badger pointed out, we were horrified at the speculation which was taking place through these purchase agreements. We did not find

anything out of the ordinary that the Government bond dealers had done. They simply pursued their own business and had their correct line and margined when they should margin and all the rest. But a whole group of speculators around the country suddenly found out that through a repurchase agreement you did not have to put up any margin. I think personally it is a terrible thing and something must be done to correct that situation.

Mr. BADGER. There is no question about it.

Senator BUSH. If the Senator would permit me, I think we should, and I presume this committee is as good as any to pursue the question and examine this speculation. At one time I called it trading against the Government in connection with new issues, and so forth. I think that is one thing. I think that can be stopped without injuring the market. On the other hand, I think we should keep in mind like these gentlemen suggested, that it is very important for the whole banking system and the whole financial world to have an active free market in Government securities so that they can call up on short notice and say I want to sell \$20 million Governments and do it over the telephone. That facilitates business and is a very important thing to be able to do. This group of 17—I am not very familiar with this group of dealers—as far as I recall, there has never been any trouble with them. They do not get into trouble. They run their business very well. They furnish a very useful and necessary service to the whole financial world. I think with that in mind, we ought to examine into the question of speculation. A lot of people speculate in these bonds. I think they are just trading against the Government. I think we ought to see if we can't do something about that.

Mr. PATRICK. It did not work so well last June.

Senator BUSH. No. Sometimes they get stung. As the chairman says, they are putting up very little and buy tremendous sums and ride it for a few points and make an enormous profit.

Mr. CONKLIN. The very fact you point out is the appeal to the speculative instinct. There are many people in the bond market who didn't know what a bond was, but just utilized it as a device to make some quick money. This is the dangerous part of the thing. It is absolutely essential to have a good market mechanism. When you get uninformed people who adopt a philosophy that stocks are old fashioned and if you want to get rich quick, buy a series of new Governments and ride them, this is dangerous. One thing that the debacle might lead to is to a lot less willingness and lot less certainty that this is the way to get rich in the future.

The CHAIRMAN. I think the life insurance people are probably the least speculative class in the community.

I hope you will join us in trying to eliminate these abuses of undue speculation in the Government bond market which I think damage their reputation.

Senator BUSH. On this point you raise about the speculation, when this committee meets in New York next week, and I hope you and I will both be able to be there, although I doubt it, the staff will see that questions are brought up with these dealers which will try to develop this question of speculation and what if anything should be done about it. It would be very helpful.

The CHAIRMAN. I hope the staff will do that.

Gentlemen, we thank you very much for coming. I am afraid you have been subjected to a long process of questioning but we appreciate your replies. We hope you will carry back to your principals the feelings that some of us have about things such as advertising and so forth.

We meet tomorrow in this same room at 10 a.m.

(Whereupon, at 12:35 p.m. the committee was recessed, to reconvene at 10 a.m. Wednesday, July 29, 1959.)

EMPLOYMENT, GROWTH, AND PRICE LEVELS

WEDNESDAY, JULY 29, 1959

CONGRESS OF THE UNITED STATES
JOINT ECONOMIC COMMITTEE,
Washington, D.C.

The committee met at 10 a.m., pursuant to recess, in the old Supreme Court chamber, the Capitol, Senator Paul H. Douglas, chairman, presiding.

Present: Senator Douglas and Representatives Patman, Widnall, and Coffin.

The CHAIRMAN. The committee will come to order.

Before we start with the witness, I would like to make a correction for the record.

Several times during the hearings I have injected the term of the rate of credit turnover or velocity on Government securities computed by the New York Clearing House Association. They testified before the Senate Committee on Banking and Currency this year that the bank deposits in the accounts of dealers in Government securities mounted to only \$35 million in February 1959, but the debits were down over \$18.8 billion in 1 month, or a monthly turnover velocity of 557 and a yearly rate of 6,683 as compared to a yearly turnover rate of approximately 32 for ordinary commercial transactions, and the monthly rate of 2.7.

I now find that subsequent to their testimony the New York Clearing House Association discovered an error in the average balances of dealers in U.S. obligations. Banking deposits in the accounts of dealers in Government securities, as corrected, were found to amount to even less than previously reported: Namely, not \$34 million but \$20 million.

On this same basis of \$20 million, the total amounts drawn amounted to over \$18.8 billion in 1 month. The monthly rate of turnover would be 938.7, and the yearly rate 11,264.

The resulting daily turnover rate, based upon 22 business days a month, is almost 43 times.

The references for this are, first, the original statement of the New York Clearing House in the Senate Banking and Currency hearings on Senate 862 and 1120, and the House Banking and Currency Committee, Subcommittee No. 2, hearings on H.R. 5237, Member Bank Reserve Requirements, pages 248-282.

This does not concern you, I know, but it is extraordinarily significant.

Representative PATMAN. Mr. Chairman, will you yield?

The CHAIRMAN. Yes, indeed.

Representative PATMAN. I think that is a good reason why we should have Central Reserve city banks. We should have a separate classification recognizing differences in the velocity of money. It is entirely different from the Reserve city banks and the country banks, and I doubt very much that consideration or adequate consideration was given those figures when we passed that recent so-called vault-cash bill.

The CHAIRMAN. As a farm boy representing the city of Chicago, I must say I cannot agree with my good friend from Texas on this point. But this is a matter that we can consider later.

Representative PATMAN. Certainly within the 3 years, I hope.

The CHAIRMAN. Mr. Ohlenbusch, we appreciate very much your coming here. We know that it interrupts a very busy life. I was a very close friend of the former president of the Bowery Savings Bank, Mr. Henry P. Bruere, and we are very glad to have you here. You may testify in your own way.

**STATEMENT OF JOHN M. OHLENBUSCH, SENIOR VICE PRESIDENT,
BOWERY SAVINGS BANK, NEW YORK CITY, ACCOMPANIED BY
SAUL B. KLAMAN, DIRECTOR OF RESEARCH, NATIONAL ASSO-
CIATION OF MUTUAL SAVINGS BANKS, NEW YORK CITY**

Mr. OHLENBUSCH. Thank you, Mr. Chairman.

My name is John M. Ohlenbusch. I am a senior vice president of the Bowery Savings Bank, New York, N.Y.

I would like to inform you, as I had earlier informed your chairman, that I am not primarily an economist and, therefore, do not feel especially qualified "in the ways in which changes in the Government's debt management operation and in the Federal Reserve System's monetary policy could improve their operation and their contributions to employment, economic growth and stable price levels." For this reason I have asked Mr. Saul B. Klamann, director of research of the National Association of Mutual Savings Banks, to accompany me on this visit with you.

I am primarily an investment man and would like to confine myself to the manner in which the Bowery Savings Bank reacts to changes in monetary and debt management policies and how these policies find reflection in the portfolio policies and operations of the Bowery Savings Bank. I hope to make certain observations on savings bank investment policies in general which might be helpful to your committee.

While disclaiming any expert knowledge in the former area, I would say that I and my associates have a deep consciousness of the public interest. Nevertheless, our first concern is the welfare of our depositors, and I must say that in our industry, as indeed must be the case in many industries, there are times when these seem to be in conflict.

One of our primary investment objectives is to maintain approximately 70 percent of assets in mortgages. Savings banks in New York State on the average maintain approximately 65 percent of assets in mortgages, and for the Nation as a whole 60 percent is so invested.

The next largest category of our investments is bonds, which constitute 26 percent of assets. U.S. Government and U.S. Government agency bonds account for approximately half of our total bond investments, or about 13.7 percent of assets. We are a trifle lower than the average savings bank in this investment category in that New York State savings banks generally have 15.9 percent so invested. The balance of our investments is in a variety of categories.

With your permission, I would like to confine myself to the 26 percent of assets constituting the bank's bond investments. I do this primarily because of my belief that bond investments are more directly concerned with the matters into which your committee is presently inquiring.

The primary function of savings banks bond investments is to provide liquidity. The need for liquidity obviously arises from a possible net outflow of deposits. A further need for liquidity arises from the manner in which many of us do our mortgage business. Most of us make substantial investments in insured and guaranteed mortgages, and for the most part these investments result from commitments made to mortgage bankers who in turn make commitments to the home builders with whom they do their business.

In general, we at the Bowery try to maintain, in addition to our cash income from all sources, a liquid fund of 7 percent of deposits. This fund consists of U.S. Government and U.S. Government agency issues maturing within 5 years. This liquid fund we like to back up by another 3 to 4 percent of assets similarly invested, maturing within 5 to 10 years.

I have given you a detailed analysis of our liquid funds because their presence, we feel, leaves us free to perform what we regard to be our primary investment mission, namely, investment in long-term obligations.

In the management of any investment account there always exists a strong temptation to try to outguess the market by buying securities when they are low and selling them when they are high. In the field of investing in bonds, this kind of policy can and frequently does lead to very substantial shifts in maturities. When prices for bonds are rising, long-term bonds will usually rise faster and further than short-term obligations. Conversely, in periods of declining bond prices or rising interest rates, long-term bonds again will travel through a much wider arc pricewise and short-term obligations afford much better protection.

Federal Reserve policy more often than not is directed at changes in short-term interest rates. Because of the fluidity of investment funds, however, and because the capital needs of business frequently coincide with the needs for short-term accommodations, long-term interest rates tend to move in the same direction as short-term rates. An institution such as ours, which might attempt to play the swings in the market in this manner, might, if successful, produce outstanding results. This has been particularly true during the postwar years when interest rates in general have been increasing. However, we have examined such a policy and have concluded that we would rather not make it a major element in our investment operations. The risks in such a program can be very substantial, especially if one should make a wrong guess and the trend in interest rates should turn differently than had been anticipated.

On the other hand, one should not conclude from this statement that we simply buy long-term bonds and always hold them to ultimate maturity. We do make considerable shifts in our investment holdings, but the manner in which we do this, we feel, involves considerably less risk to our depositors.

Without changing substantially our overall maturity distribution, we will at times make important shifts from one class of securities to another. Immediately following the war, for instance, our bond investment portfolio was mostly in U.S. Government securities. Since that time Government bond holdings have been reduced and other types of investments have been increased.

However, there have been three or four times during these years when we have regarded it advisable to shift out of substantial amounts of our other bond holdings to purchase U.S. Government obligations.

I must say that in doing this we have been prompted by what we believe to be in the best interest of our depositors but we also believe that functioning in this manner we have made a contribution to the Treasury's debt management policies without running contrary to the monetary policies of the Federal Reserve.

My written statement contains two hypothetical cases showing the manner in which the investment arithmetic of these operations is determined and their results appraised. This is done by reference to examples using a hypothetical corporate bond and a hypothetical Government bond. Our investment operations in this area, however, have not been confined to these two types of obligations. This kind of thing can be done with any two securities or groups of securities and, indeed, is very frequently done between one issue of U.S. Government security and another.

The results flowing from such transactions in a rising and in a falling bond market are set forth in exhibit III.

Earlier I had said that the way to invest profitably is to buy securities when they are low and sell them when they are high. That is precisely what we attempt to do, except that what is "high" or "low" is determined by the price or yield of what we are buying in substitution. In U.S. Government securities we have a security without risk as to credit. All other obligations to greater or lesser degrees reflect some element of credit risk. These Government bonds become an excellent yardstick against which other securities may be measured.

At the Bowery we have recently completed a review of the results obtained from managing our portfolio in this manner. These results, as percentages of the average amount invested, are attached to my written statement as exhibit IV. To summarize, we have determined that the increasing income received from securities (a large portion of which has resulted from these switching operations) has been almost enough to offset the losses we have taken. From this point on, our income from securities is going to be substantially higher than would otherwise have been the case. Furthermore, we have determined that the depreciation, had we done nothing, has exceeded the depreciation existing in the account at the end of last year by 6.55 percent.

We think the economic consequences of what we have been doing with our bonds have been good. Since so many of those transactions have involved U.S. Government securities, either on the buy or sell

side, we think a real contribution has been made to the Treasury's debt management program. When corporate bonds, for instance, have been at their highest price relative to Governments, it has usually been at periods immediately following flotations of new long-term securities by the Treasury. These periods have frequently found us selling corporates to buy Governments and in effect sustaining that market.

On the other hand, when the Treasury has not been in the market for some time with a new long-term offering, and when flotations of new corporate securities are heavy, we have become sellers of Governments and purchasers of corporates.

We think this program has been of benefit to the Bowery Savings Bank, has not been inconsistent with the monetary objectives of the Federal Reserve Board, and has been of assistance to the Treasury in its debt management problem.

Just one thing remains to be discussed. None of us wants to return to the era when the Federal Reserve System was pegging the Government bond market and taking nearly unlimited quantities of long-term bonds at a fixed price. Much thoughtful consideration has been given, however, as to whether the Federal Reserve System should not assist the Treasury's debt management problems by purchasing U.S. Government securities of varying maturities.

I assume here that such a program would not involve additional debt monetization, in that such purchases might be offset with sales of Treasury bills or changes in reserve requirements. I believe the thought is that such action would permit the Treasury to float new issues of long-term bonds at lower rates than would otherwise be the case. I do not think that such efforts would be in the Nation's best interests or that they would be successful. Let me give you my reasoning on this score.

The subject seems to divide itself into two parts: First, one might take the view that such action would tend to keep all long-term rates lower or, second, that such action might create a favored market for Treasury securities.

Fundamentally, such a policy is price fixing of a very dangerous type. Interest rates are nothing by the expression of the price of money. Interference with this price, as in the case of any price fixing, interferes with the normal functioning of the price mechanism.

What are the effects of the rising price for money? First of all, higher rates are likely to induce new savings that might not otherwise have been created. Second, and this seems much more important, savings already accumulated may be prevented from being used in an inflationary manner resulting in an unsustainable level of economic activity.

One example of this kind of thing is to be found in the stock market. Let us assume that I own a block of stocks purchased some years ago. John Doe, impressed with the record made by the stock market in recent years, buys my stocks and pays cash for them. I suddenly find myself with a lot of money that I did not have before, but since this money came easily, I indulge myself in some luxury that otherwise I could ill afford. Moreover, it is not even necessary to have an actual stock transaction for the influence of rising stock prices to make itself felt on the economy. The mere fact that my stocks are rising gives me the feeling that I can now afford to spend more freely.

It should be noted that in neither of these cases has any credit been involved, but is this kind of unsustainable economic activity which increasing interest rates on long-term securities will prevent.

I know that in this matter of allowing the price of money to increase many worthwhile projects may become casualties or will have to be postponed. This again is a result of the normal functioning of the price mechanism, but it is not all bad. As in the case of a rise in the price of any other commodity, people start using their ingenuity, and substitute products are found. New methods are devised. Some of these turn out to be more than mere makeshift substitutes and eventually find a permanent place in our economy.

None of us likes high-interest rates per se. We would prefer not to have to postpone the satisfaction of some of these wants. It is easier if we do not have to exercise our ingenuity in the development of new, less costly substitutes, but these are salutary results much to be preferred to constantly rising prices or to encouraging the unsustainable economic expansion which all of us seek to avoid.

A further possible danger inherent in the Fed's influencing long-term yields may be pointed up by reference to the events which took place in the bond market in the early part of 1958. In the spring of that year there were divided viewpoints on the proper level of long-term interest rates. A most reliable person, with the benefit of economic counsel of the highest order, expressed the view that long-term interest rates should have been 1 percent lower than was actually the case.

On the other hand, there were others who felt that, while we were in a temporary recession, the long-range economic problem of the Nation still was the control of inflation. This later, too, appeared to be the view taken by the marketplace as expressed in the price for money. Suppose the Federal Reserve Board, however, had adopted the former point of view and in pursuit of the policy under consideration had been successful in lowering long-term yields by the 1-percent mention. This would have meant an additional rise of 20 points over the prices then prevailing for long-term Government bonds.

We know now that throughout the closing months of 1957 and in the first half of 1958 a most undesirable situation was created in the Government securities market. How much worse would it have been, had the power of the Federal Reserve System been behind this move. We also knew that in July of 1958 the Treasury and the Federal Reserve bought \$650 million of securities to avert disorderly conditions in the Government bond market. These purchases restored order, but I know of no one who holds that the subsequent decline has been any less because of these purchases. If purchases in this quantity were insufficient to change the ultimate course of the long-term market, who can say how much would have been necessary had the market started at a level 20 points higher?

If we can be in agreement that the Federal Reserve should not conduct itself so as to influence directly the level of long-term interest rates, is there not something the Federal Reserve might do to give assistance to the market for long-term Government securities? Can it not to a degree at least create a preferential situation in the market for the Treasury?

Let us assume a market condition under which long-term Governments are selling to yield 3.5 percent and long-term corporates are selling to yield 4 percent. Here we have what might be considered a

normal spread between these two types of obligations. Let us assume further that economic conditions are such that it is the decision of the Board of Governors of the Federal Reserve System to allow the money market to tighten, and under such a program the corporate market might be expected to decline in price to the point where the going rate on corporate bonds would be 4½ percent.

In a completely free market it can be assumed that long-term Government bonds would decline in price similarly and afford a yield of 4 percent, again keeping our so-called normal relationship. However, under its program of giving a measure of support to the long-term Government market, the Fed decided that these bonds should be allowed to decline only to the point where they yield 3.75 percent. Our spread between Governments and corporates has now widened to 0.75 percent. Under our bank's policy of acting on these relationships, we would become sellers of Government securities and buy corporates. The Fed's problem of maintaining Governments at the 3.75 level would become just that much more difficult. But even if we were not to take advantage of the situation thus created by the Fed, and if all other long-term investors similarly refrained from taking advantage of this situation, what would be the circumstances?

I have put this case to you in terms of what the Bowery Savings Bank does, but let us assume that no one took advantage of the condition created by the Fed and the Secretary of the Treasury decided that this was an opportune moment to sell new long-term bonds. We at the Bowery are not the only ones watching these relationships, although we may be among the few taking advantage of them in what is called the secondary market as opposed to the market for newly issued securities. Investors with new funds would have the option of purchasing either the Treasury's new offering at 3.75 percent or purchasing high-grade corporates to yield 4.5 percent. What investment manager acting on behalf of his clients would choose the Government bond as against the corporate? The Treasury might sell a few long-term bonds to unsuspecting investors, but would the amount be sufficient to help the Treasury in its debt-management problem? Would the investors so mousetrapped be willing buyers of the Treasury's offering the next time?

What we need is more friends for Treasury bonds, not fewer.

The CHAIRMAN. Thank you very much.

At this point, without objection, your prepared statement will be placed in the record in its entirety.

(The statement referred to follows:)

STATEMENT OF JOHN M. OHLENBUSCH, SENIOR VICE PRESIDENT, BOWERY SAVINGS BANK, NEW YORK CITY

My name is John M. Ohlenbusch. I am a senior vice president of the Bowery Savings Bank, New York, N.Y. A list of the trustees and officers of the Bowery Savings Bank is attached hereto as exhibit I.

The Bowery Savings Bank is a mutual savings bank chartered in 1834 and operates under the banking law of the State of New York. The bank accepts deposits from individuals and fiduciaries of funds up to \$10,000 for each. The banking law also permits acceptance without limitation of deposits from recognized religious and charitable organizations. Savings banks accept no demand deposits. Under the banking law the trustees of the bank may require 60 days' notice for withdrawal of deposits but, as a practical matter, the Bowery Savings Bank and savings banks generally have not required such notice since the period immediately following the bank holiday in 1933. The bank is under the super-

vision of the superintendent of banks of the State of New York and is a member of the Federal Deposit Insurance Corporation.

The bank's investments are limited to those categories authorized in the New York State banking law which include certain bonds made eligible by the banking board and certain limited investments not otherwise eligible.

As exhibit II there is presented a rather more detailed statement than is generally provided to the public, showing the bank's position as of June 30, 1959.

At the outset, I would like to inform you, as I had earlier informed your chairman, that I am not primarily an economist and, therefore, do not feel especially qualified "in the ways in which changes in the Government's debt management operation and in the Federal Reserve System's monetary policy could improve their operation and their contributions to employment, economic growth and stable price levels." For this reason, I have asked Mr. Saul B. Klamman, director of research of the National Association of Mutual Savings Banks, to accompany me on this visit with you.

I am primarily an investment man and would like to confine myself to the manner in which the Bowery Savings Bank reacts to changes in monetary and debt management policies and how these policies find reflection in the portfolio policies and operations of the Bowery Savings Bank. I hope to make certain observations on savings bank investment policies in general which might be helpful to your committee. While disclaiming any expert knowledge in the former area, I would say that I and my associates have a deep consciousness of the public interest. Nevertheless, our first concern is the welfare of our depositors and I must say that in our industry, as indeed must be the case in many industries, there are times when these seem to be in conflict.

What I am going to tell you about the Bowery Savings Bank investment policy may or may not be found in the records of that bank. Some of it is contained in the minutes, but much of it shows itself only in the manner in which our affairs are conducted.

You will note from exhibit II, lines 33 to 38, that real estate mortgage loans constitute 67 percent of our assets. You will note further that ship mortgage loans, line 39, constitute another 2.6 percent of assets. These latter are all loans guaranteed by the U.S. Government under title XI of the Merchant Marine Act. Our policy objective is to maintain approximately 70 percent of assets in these two categories. Savings banks in New York maintain approximately 65 percent of assets in real estate loans, and for the Nation as a whole 60 percent is so invested.

The savings bank law in New York State places an overall limitation on so-called conventional real estate loans of 65 percent of assets. No mention is made in this law regarding any limitation on federally insured or guaranteed loans. Under the law, therefore, a New York savings bank might have practically all its assets invested in mortgage loans, provided the amount in excess of 65 percent is federally insured or guaranteed. Since so many of our loans are federally insured and guaranteed, and in consideration of their amortizing nature, we have thought that 70 percent of assets in mortgages would be appropriate and, indeed, at times have given consideration to increasing this amount.

The next largest category of our investments is bonds which you can see from line 29 of the exhibit constitutes 26 percent of assets. U.S. Government and U.S. Government agency bonds account for approximately half of our total bond investments, or about 13.7 percent of assets. We are a trifle lower than the average savings bank in this investment category in that New York State savings banks, generally, have 15.9 percent of assets so invested. As you can see, we have the balance of our bond investments in the various categories listed on lines 22 to 29.

With your permission, I would like to confine my remarks to the 26 percent of assets constituting the bank's bond investments. There are several reasons for my wanting to do this. First, this is the field in which I am primarily qualified. My associate, Mr. Held, who has appeared before other congressional committees, is infinitely more qualified in mortgage investments than I would be. Secondly, bond investments are more directly concerned with the matters into which your committee is presently inquiring. Third, this area creates a more interesting problem for discussion because of the diversity of policies and results.

As an indication of this last factor, I would like to point out to you some statistics for the Manhattan and Bronx savings banks of assets of \$200 million or more. For 1958 the bank with the best earnings on real estate mortgages

had a return of .37 percent above the bank showing the lowest earnings in this field. In the case of Government bonds, however, the bank with the highest earnings had a return of 0.72 percent above the bank with the lowest earnings in this investment area. A similar conclusion could be drawn from an analysis of the earnings of all savings banks in New York State. It is this wider earnings disparity in the case of bonds that makes them the more interesting problem to me.

The primary function of the bond investment category of savings bank assets is to provide liquidity. The need for liquidity obviously arises from a possible net outflow of deposits. A further need for liquidity arises from the manner in which many of us do our mortgage business. As you can see from our statement, the bulk of our mortgage investments is in the insured and guaranteed field. For the most part these investments result from advance commitments made to mortgage bankers who have applied for such commitments on behalf of the homebuilders with whom they do their business. These commitments usually involve periods of a year or more and may run for as long as 2 years. Our ship loan activities at times will involve commitments for as long as 3 years. While we have only \$46 million invested in this field at the present time, our commitments amount to another \$75 million. Our commitments in the real estate field on June 30 amounted to \$147 million. As you can appreciate, this commitment position requires careful scheduling against our cash income from all sources but, as it relates to our bond investments, emphasizes the need for a substantial liquid fund.

In general, we try to maintain, in addition to our cash income from all sources, a liquid fund of 7 percent of deposits. This fund consists of U.S. Government and U.S. Government agency issues maturing within 5 years. It also includes our holdings of nonmarketable Government securities, since these are redeemable by the Treasury on relatively short notice. We also include in this category our holdings of U.S. Treasury nonmarketable 2¾s, 1975-80, which are convertible into 5-year 1½ percent Treasury notes. Against all these nonmarketable and convertible securities, we maintain valuation reserves to the redemption prices or, in the case of the 1½ percent 5-year notes, the lowest market price at which these obligations have sold.

In the marketable category, from time to time we will have rather substantial—for us—Treasury bill holdings if our commitment and deposit outlook indicates this to be necessary. At other times, this fund has also included substantial amounts of Government agency issues in the maturity category of 1 year or less.

This liquid fund we like to back up by another 3 to 4 percent of assets in U.S. Government or Government agency obligations maturing within 5 to 10 years. At the present time, this fund is divided about equally between Governments and Government agencies.

I have given you a rather detailed explanation of our liquid funds position and needs because I think they have an important bearing on our other investment policies. With the presence of these funds, we have felt quite free to perform what we regard to be our primary investment mission, namely, investment in long-term obligations.

In the management of any investment account there always exists a strong temptation to try to outguess the market by buying securities when they are low and selling them when they are high. In the field of investing in bonds, this kind of a policy can, and frequently does, lead to very substantial shifts in maturities. When prices for bonds are rising, long-term bonds will usually rise faster and further than short-term obligations. Conversely, in periods of declining bond prices or rising interest rates, long-term bonds again travel through a much wider arc and short-term obligations afford much better protection.

Federal Reserve policy, more often than not, operates so as initially to affect changes in short-term interest rates. Because of the fluidity of investment funds, however, and because the capital needs of business frequently coincides with its needs for short-term accommodations, long-term interest rates tend to move in the same direction as short-term rates. Thus, Federal Reserve policy which might call for a condition under which the short-term money market might be allowed to tighten itself, will frequently find reflection in the capital markets. An institution such as ours which might attempt to play the swings in the market in this manner might, if successful, produce outstanding results. This has been particularly true during the postwar years when interest rates in general have been increasing. However, we have examined such a policy

and have concluded that we would rather not make it a major element in our investment operations. The risks in such a program can be very substantial, especially if one should make a wrong guess and the trend in interest rates should turn differently than had been anticipated.

On the other hand, one should not conclude from the above statement that we simply buy long-term bonds and hold them to ultimate maturity. We do make considerable shifts in our investment holdings, but the manner in which we do this, we feel, involves considerably less risk to our depositors.

Without regard to changing substantially our overall maturity distribution we will, at times, make important shifts from one class of securities to another. The beginning of the postwar era, for instance, found us with a bond investment portfolio mostly in U.S. Government securities. Since that time, our Government bondholdings have been reduced both in quantity and even more substantially as a percentage of total assets. However, there have been three or four times during these years when we have regarded it advisable to shift out of substantial amounts of other bondholdings to purchase U.S. Government obligations.

At the outset, I must say that we have been prompted in these actions by what we believe to be the best interest of our depositors, but we also believe that functioning in this manner we have made a contribution to the Treasury's debt management policies, without running contrary to the monetary policies of the Federal Reserve.

Let me explain by reference to two hypothetical cases how this sort of thing works advantageously. The first case I am going to give you is, we might say, an idealized version of our objective which will set forth clearly the profit to be gained in this kind of operation. The second case will be more typical of what has happened in postwar years when, in general, interest rates have been rising and bond prices have been declining.

To illustrate the first case, let us assume that we own the bonds of the XYZ corporation and that these bonds are 3 percent bonds due in 20 years. These bonds were purchased by the bank at par and are currently selling in the market at this same price. Let us assume now that the U.S. Treasury sees fit to offer a 20-year bond in the market and concludes that the proper offering price for such a security is par for a 2½-percent bond to yield 2.75 percent. Secretary Anderson, in a previous appearance before your committee, demonstrated how the issuer of new debt securities has to offer his obligations at somewhat of a discount or at a little better rate than outstanding obligations. He also stated very clearly why this is necessary.

Under our investment policy we have been investing our funds in long-term securities as they were received. We have not been accumulating any large sums in anticipation of the Treasury's offering of long-term securities. However, knowledge of the past relationships between different classes of bonds indicates that here is an opportunity for a profit. We therefore sell the bond of the XYZ corporation at par and we purchase the Treasury's 2½-percent bond. In the light of the history of the relationship between Treasury obligations and high-grade corporate obligations this spread in yield of one-quarter of 1 percent, or 25 basis points as we refer to it, is too narrow. In all probability it will widen out to somewhere nearer 50 basis points and, possibly even more. Without regard to the intervening time necessary for these bonds to readjust themselves, let us assume now that the spread has widened out to our desired 50 basis points or one-half of 1 percent in yield. This could mean that our Treasury bond, which was purchased at par, is now selling to yield 2.50 percent and, at this price, can be sold at 103.92. Our XYZ corporate 3-percent bond can be repurchased at par. Our income from now on is the same 3 percent that it was before the XYZ corporate bond was sold and we have made a profit in the Treasury obligation of 3.92 percent. This calculation, of course, presupposes no lapse of time between the two transactions and no allowance has been made for the lower income while holding the Treasury obligation. These things, of course, do not happen simultaneously as I have described, but the assumption of the simultaneous transaction serves to point up the benefit.

In addition to the disregard of the lapse of time, these transactions never work out as ideally and as simply as I have stated the case above. More frequently these transactions have involved the taking of losses rather than the taking of profits, because, since 1946, generally speaking, we have been in a declining bond market. This is how the above transaction might work out in a declining market. Our XYZ 20-year, 3-percent corporate bond might have been purchased at par and sold at a price to yield 3.25 percent, a price of 96.34.

Our assumption as to the spread in yield calls for the purchase of a 20-year Treasury 3½-percent bond at par. It will be noted that in this transaction we have the same spread between the two bonds of 25 basis points as we had in the prior case. Now again, disregarding the lapse of time, let us assume a continuation of the decline in the bond market with a widening in the spread between our corporate obligation and the Treasury bond. Let us now assume that we can sell our Treasury bond at a 3.75-percent yield or a price of 96.50. Under the assumption that the spread between the two bonds has widened to a half of 1 percent, or 50 basis points, our corporate bond can be purchased to yield 4.25 percent or at a price of 83.27.

Reviewing this transaction we can see that in the sale of our corporate bond we had to take a loss of 3.66 points. When we sold the Treasury bond we took a further loss of 3.50 points. The total losses we have taken thus amounted to 7.16 points. Furthermore, as in the previous transaction, we have been able to take cash out of our investment. Thus, when we sold the corporate bond at 96.34 and bought the Treasury at par, \$3.66 (per hundred dollars of investment) had to be added to our investment. In the second set of transactions, however, our sale was made at 96.50 and the repurchase of the corporate bond was made at 83.27. At this point, we were able to take 13.23 points out of our investment. Thus, we have available net cash of 9.57 points. We have had total losses amounting to 7.16 points but, instead of having the corporate bond on our books to yield us 3 percent, we now have the corporate bond on our books to yield 4.25 percent. Our future income is going to be considerably larger.

There is one further advantage in this kind of operation and it comes about as follows: In the case I have just described to you, the market value of the corporate security involved here declined from the price at which it was purchased of 100 all the way down to 83.27. It has declined in price by 16.73 points while we took losses of only 7.16 points. Thus we conclude that we have avoided depreciation of 9.57 points.

Balance sheets reflecting an assumed bank's position before and after each of the transactions involved in the two cases are presented as exhibit III.

This latter case, as I have said, more nearly exemplifies how this business of shifting from one security to another has worked in recent years. The case I have cited was one involving corporate bonds and U.S. Government bonds. In our investment practices we have not confined our activities only to these two groups. This kind of thing is possible as between State and municipal bonds on the one hand and Governments on the other. We have been doing it, with some degree of success, with Government agency obligations and treasury bonds. Opportunities have arisen as between one issue of U.S. Government bonds and another.

Earlier I had said that the way to invest profitably is to buy when securities are low and sell them when they are high. That is precisely what we are trying to do except that "high" or "low" is determined by the price or the yield of what we are buying in substitution. In U.S. Government securities we have a security without risk as to credit. All other obligations, to greater or lesser degrees, reflect some element of credit risk. Thus, Government bonds become an excellent yardstick against which other securities may be measured.

We recently thought it might be interesting to make a review of our portfolio as it was managed in the postwar years, giving effect to these losses and to the income we have derived from our securities holdings. This has been done for the years 1946 through 1958 and is presented herewith as exhibit IV. The first column of this table shows the operating income the bank has derived from securities (for most years, the coupon interest, less the amortization of premium or discount). The second column shows the net bond profits or losses. The third column combines the first two to show the net income. Thus, net income, after deducting losses, has been at the average annual rate of 2.43 percent. At the beginning of this period the bank's operating income from securities was at the rate of 2.44 percent. Thus, if we had done nothing other than hold the securities which were in our portfolio on January 1, 1946, we would have had a return which was almost identical with the return, after deducting losses, as the portfolio was managed. The reason, of course, was that the willingness to accept the losses permitted the bank to increase its operating income from securities from the initial 2.44 percent to the average of 2.71 percent for the 13-year period. Our operating income from securities at the end of 1958 stood at 3.57 percent in contrast to the 2.44 percent at the beginning of the period covered. In other words, had this program been stopped at the end of 1958 we could have concluded that substantially all of our losses had been made up by

increased income and from that point on we would be able to enjoy an income of 1.13 percent more than it was at the beginning of the period.

At the end of 1958 the unrealized depreciation existing in our bond investment account amounted to 5.45 percent of the funds so invested. Had the bank done nothing throughout this period and retained its 1946 investments, it is estimated that the depreciation would have amounted to more than 12 percent. Just as in the hypothetical case described to you previously there was indicated a measure of market depreciation which had been avoided, similarly, here with the overall management of our account, the market depreciation which has been avoided can be estimated at 6.55 percent.

So much for the benefits to the Bowery Savings Bank derived from this kind of operation in bond investments. What are the broader implications? What are the economic effects of what we have been doing?

We think they have been good. Since most of these transactions have involved U.S. Government securities, we think a real contribution has been made to the Treasury's debt management program. When corporate bonds have been at their highest price relative to Governments, it has usually been at periods immediately following flotations of new long-term securities by the Treasury. These periods have frequently found us selling corporates and in effect sustaining the Government bond market. On the other hand, when the Treasury has not been in the market for a long period with a new long-term offering, and when flotations of new corporate securities are heavy, we have become sellers of Governments and purchasers of corporates.

We think this program has been of benefit to the Bowery Savings Bank, has not been inconsistent with the monetary objectives of the Federal Reserve Board and has been of assistance to the Treasury in its debt management problem.

Just one thing remains to be discussed. I am sure no one would advocate the return to the era when the Federal Reserve System was pegging the Government bond market and taking nearly unlimited quantities of long-term bonds at a fixed price. Much thoughtful consideration has been given, however, as to whether the Federal Reserve System should not assist the Treasury's debt management problems by purchasing U.S. Government securities of varying maturities. I assume here that such a program would not involve additional debt monetization in that the Fed would offset purchases of long-term bonds with sales of Treasury bills or changes in reserve requirements thereby leaving unchanged total Federal Reserve bank credit. I believe the thought is that this action would permit the Treasury to float new issues of long-term bonds at a lower rate than would otherwise be the case. I do not think that such efforts would be in the Nation's best interests or that they would be successful. Let me give you my reasoning on this score.

Fundamentally such a policy is price fixing of a very dangerous type. Interest rates are nothing but the expression of the price of money. Interference with this price, as in the case of any price fixing, interferes with the normal functioning of the price mechanism.

The Treasury has recently had to pay 4.75 percent for 4¾-year money. This happened to be on a refunding but the arguments are just as persuasive had this represented the borrowing of new money. Why would not 4.25 percent or even 3.75 percent have done as well?

The answer is relatively simple. First of all, the 4.75 percent was the rate necessary to compete with other money market instruments. In our economy the Treasury is not a preferred borrower. Fundamentally, however, these rates are only the technical reflections of the state of economic affairs in which the demands for funds are pressing against the available supply. What are the salutary effects of the higher level of rates resulting from the interplay of free-market forces? First of all, higher rates are likely to attract new savings that might not otherwise have been created. Second, and of much more importance, savings already accumulated may be prevented from being used in an inflationary manner so as to result in an unsustainable level of economic activity.

One example of this kind of thing is to be found in the stock market. True, the amount of credit being extended in this area is relatively minor but credit is not the only means by which unsustainable economic activity may be created. A simple example will demonstrate the point. Let us assume that I own a block of common stocks purchased years ago. John Doe, impressed with the record made by the stock market in recent years, buys my stocks and pays cash for them. I suddenly find myself with a lot of money that I did not have before, but since this money came easily, I decide to buy a second automobile which I can assure you I do not need and could otherwise ill afford.

Moreover, it is not even necessary to have an actual stock transaction for the influence of rising stock prices to be felt in the economy. The mere fact that my stocks are rising gives me the feeling that I can now afford to spend more freely.

This is the kind of unsustainable economic activity which we should try to avoid. It is hopeful that the rate of 4.75 percent on Government bonds will dissuade John Doe from buying my stocks and thus financing my unneeded second automobile. If it does not, then the rate on Government securities must go still higher.

I know that in this matter of allowing interest rates to increase, many worthwhile projects may become casualties or will have to be postponed. As a member of the school board in my community, I am deeply conscious of our need for schools and the very best educational system we can possibly afford. Let me tell you of a recent experience we went through at one of our meetings which has a remote yet very important bearing on what we are talking about.

We had been deeply impressed by a recent report on the public high school system which, among other excellent recommendations, pointed up the inadequacy of the general level of instruction in English. To cure this, the report recommended a maximum pupil load of 100 for English teachers. It went on to say that throughout their high school careers children should be required to submit a written composition at least once a week. Our English teachers were carrying well in excess of 100 pupils each but I am proud to say that for many years had been requiring the written work called for in the report. We discussed whether or not with our recently expanded high school we could institute such a program in the English department. The figures soon indicated that if we wished to do this, we would have to hire new teachers and, furthermore, we would again have to ask for additional high school facilities.

The community in which I live happens to command a high credit rating but I know that we would have to pay very close to 4 percent to borrow at this time.

I do not think we are the only community confronted with this kind of a problem. From an article in the New York Herald Tribune of July 19, 1959, it is noted that the research staff of the Educational Testing Service of Princeton, N.J., has come out with a plan suggesting the use of "lay readers," competent housewives who might assist English teachers by correcting papers at home. Sixteen school systems are already using this program and by so doing have been able to increase the teacher load to 200 pupils. As one interested in education, I should put this the other way round; such a system permits 200 pupils to be exposed to the really competent English teacher. Class sizes have been considerably increased presumably with an improved English program. Incidentally, the need for additional classrooms is also reduced.

I point this out not because I think high or freely fluctuating interest rates are the answer to our education problems. It is pointed out merely as an example of the manner in which the free price system for money, as indeed for all commodities, is a factor leading to increased efficiency not only in the educational field but in all fields.

None of us likes high interest rates per se. We would prefer not to have to postpone the financing of essential municipal projects, including schools. But what is the alternative? If interest rates were lower, we would be encouraging the unsustainable economic expansion which all of us want to avoid.

Now let us examine the proposal to influence Government bond yields in terms of some of the events that were taking place in the bond market in 1958. I have in mind that in the spring of that year there were sharply divided viewpoints on the proper level of long-term interest rates. A most reliable person, who had the benefit of economic advice of the highest order, was of the opinion that he could not understand why long-term interest rates were not 1 percent lower than was actually the case. On the other hand, there were others who felt that, while we were in a temporary recession, the long-range economic problem of the Nation still was the control of inflation. Suppose the Federal Reserve Board, however, had adopted the former point of view and the long-term Government bond market had been put up another 21 points¹ in reflection of a lowering of long-term yields by the 1 percent mentioned. We know now that throughout the closing months of 1957 and the first 6 months of 1958 a most undesirable situation was created in the Government securities market. We also know that in July of 1958 the Treasury and the Federal Reserve System in

¹ As measured by a 32-year 3½-percent bond as offered by the Treasury early in 1958.

combination bought \$650 million to avert a disorderly condition in the Government securities market. Order was restored by these purchases but I know of no one who holds that the decline in the bond market since that time has been any less because of these purchases. If \$650 million of purchases were insufficient to change the ultimate course of the bond market, who can say how much would have been necessary?

I would certainly not disagree with anyone who would say that the June-July decline in Government securities was caused by an unfortunate technical position in that market. Nevertheless I hesitate to think of what the technical position of the market might have been had it been known throughout the late winter and early spring of 1958 that the Fed was actively buying longer maturities as it was pursuing its program of monetary expansion. What kind of a situation might we have had on our hands now had the long-term bond market been 20 points higher in June 1958?

If we can be in agreement that the Federal Reserve should not conduct itself so as to influence directly the level of long-term interest rates, is there not something the Federal Reserve might do to give assistance to the market for long-term Government securities? Can it not to a degree at least create a preferential situation in the market for the Treasury?

Let us assume a market condition under which long-term Governments are selling to yield 3.50 percent and long-term corporates are selling to yield 4 percent. Here we have what might be considered a normal spread between these two types of obligations. Let us assume further that economic conditions are such that it is the decision of the Board of Governors of the Federal Reserve System to allow the money market to tighten and under such a program the corporate market might be expected to decline in price to the point where the going rate would be $4\frac{1}{2}$ percent. In a completely free market it can be assumed that long-term Government bonds would decline in price similarly and afford a yield of 4 percent, again keeping our so-called normal relationship. However, under its program of giving a measure of support to the long-term Government market, the Fed decided that these bonds should be allowed to decline only to the point where they yield 3.75 percent. Our spread between Governments and corporates has now widened to 0.75 percent. Under our bank's policy of acting on these relationships, we would become sellers of Government securities and buy corporates. The Fed's problem of maintaining Governments at the 3.75 level would become just that much more difficult. But even if we were not take advantage of the situation thus created by the Fed, and if all other long-term investors similarly refrained from taking advantage of this situation, what would be the circumstances?

I have put this case to you in terms of what the Bowery Savings Bank does, but let us assume that no one took advantage of the condition created by the Fed and the Secretary of the Treasury decided that this was an opportune moment to sell new long-term bonds. We at the Bowery are not the only ones watching these spreads although we may be among the few taking advantage of them in what is called the secondary market as opposed to the market for newly issued securities. Investors with new funds would have the option of purchasing either the Treasury's new offering at 3.75 percent or purchasing high-grade corporates to yield 4.50 percent. What investment manager acting on behalf of his client would choose the Government bond as against the corporate? The Treasury might sell a few long-term bonds to unsuspecting investors but would the amount be sufficient to help the Treasury in its debt management problem? Would the investors so mousetrapped be willing buyers of the Treasury's offering the next time?

What we need is more friends for Treasury bonds, not fewer.

THE BOWERY SAVINGS BANK

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EXHIBIT II

Statement of condition as of June 30, 1959

ASSETS

		Percent to total assets	
		June 30, 1959	June 30, 1958
1. Cash on hand.....	\$3,732,156.34	0.21	0.23
2. Due from banks and trust companies:			
3. Bankers Trust Co.....	\$855,488.38		
4. Bank of New York.....	300,000.00		
5. Chase Manhattan Bank.....	1,443,071.30		
6. Hanover Bank.....	977,017.90		
7. Chemical Corn Exchange Bank.....	818,320.32		
8. Commerical Bank of North America.....	31,239.74		
9. Fiduciary Trust Co. of New York.....	300,000.00		
10. Irving Trust Co.....	1,800,495.01		
11. Manufacturers Trust Co.....	100,000.00		
12. Marine Midland Trust Co. of New York.....	250,000.00		
13. Morgan Guaranty Trust Co.....	1,275,000.00		
14. First National City Bank of New York.....	1,503,299.71		
15. New York Trust Co.....	150,000.00		
16. Savings Banks Trust Co.....	555,937.68		
17. United States Trust Co. of New York.....	150,000.00		
18. Certificates of Deposit Savings Banks Trust Co.....	10,000,000.00		
	20,509,870.04	1.17	1.38
19. Bonds:			
20. U.S. Government.....	208,876,475.57	11.85	13.14
21. U.S. Government Agencies.....	34,019,821.30	1.93	2.15
22. International Bank.....	34,369,364.28	1.95	2.08
23. New York State and subdivisions, including revenue.....	19,479,609.48	1.10	1.31
24. Other States and subdivisions, including revenue.....	19,692,233.04	1.12	1.04
25. Railroad.....	39,297,208.55	2.23	2.21
26. Public utility.....	41,849,108.57	2.37	2.29
27. Industrial.....	46,838,821.81	2.65	2.68
28. Institutional Securities Corp., debentures.....	3,267,000.00	.19	.27
29. Canadian.....	14,652,348.22	.83	.83
	462,341,990.82	26.22	28.00
30. Stocks:			
31. Preferred.....	1,142,941.67	.06	0
32. Common.....	7,877,884.89	.45	0
	9,020,826.56	.51	0
33. Mortgage loans:			
34. Conventional.....	185,987,668.27	10.55	11.12
35. Federal Housing Administration.....	390,797,642.93	22.16	21.64
36. Truited mortgages, participations.....	6,476,869.66	.37	.42
37. Veterans' Administration, full guaranteed.....	4,249,240.94	.24	.29
38. Veterans' Administration, partly guaranteed.....	595,200,258.81	33.76	33.63
	1,182,711,680.61	67.08	67.10
39. Ship loans.....	46,468,518.88	2.64	.97
40. Stock and debentures, Savings Banks Trust Co. and Institutional Securities Corp.....	3,960,000.00	.22	.23
41. Housing Corporation.....	257,380.00	.01	.16
42. Certificates of investment, savings banks life insurance.....	170,000.00	.01	.01
43. Promissory notes, secured.....	410,872.26	.02	.01
44. Banking houses and leasehold improvements.....	14,692,041.96	.83	.87
45. Furniture and equipment.....	343,432.89	.02	0
46. Other real estate.....	15,959.24	0	.01
47. Interest due and accrued (less reserve of \$36,558.60).....	12,945,068.06	.74	.71
48. Accounts receivable.....	1,600,347.67	.09	.05
49. Mortgage loans in process.....	285,110.83	.02	.06
50. Prepaid expenses.....	484,225.17	.03	.03
51. Acquisition costs on mortgage loans.....	2,927,462.64	.17	.17
52. Mortgagors' and tenants' securities held in escrow (contra).....	\$5,866,825.00		
53. Less contra account.....	5,866,825.00		
	0	0	0
54. Other assets.....	206,126.11	.01	.01
55. Total.....	1,763,083,070.08	100.00	100.00

EXHIBIT II—Continued
LIABILITIES, SURPLUS AND RESERVES

		Percent to total assets	
		June 30, 1959	June 30, 1958
56. Due 579,331 depositors (includes 44,888 school, 22,506 Christmas club).....	\$1, 570, 006, 677. 25	89. 04	89. 24 ¹
57. Previous month, due 580,455 depositors— \$1,563,023,580.50.....			
58. Special deposits.....	5, 518, 546. 21	. 31	. 29 ¹
59. Mortgagors' accounts.....	6, 927, 889. 91	. 39	. 39
60. Accounts payable.....	3, 687, 221. 41	. 21	. 18 ¹
61. Due Federal Reserve bank.....	196, 612. 50	. 01	. 01
62. Security and escrow deposits.....	204, 763. 27	. 01	0
63. Prepaid interest.....	5, 755. 94	0	0
64. Unearned discount, mortgage loans.....	17, 619, 336. 95	1. 00	. 87 ¹
65. Unearned income and discount, other.....	83, 082. 67	. 01	. 01
66. Accrued for taxes and expenses.....	635, 392. 26	. 04	. 03 ¹
67. Reserve for bonds.....	3, 314, 298. 00	. 19	. 35 ¹
68. Reserve for bonds, accumulated discounts.....	574, 261. 60	. 03	. 01
69. Reserve for bonds, premiums.....	2, 207, 362. 38	. 13	. 17 ¹
70. Reserve for stocks.....	36, 472. 55	0	0
71. Reserve for mortgage loans, acquisition costs.....	2, 927, 462. 64	. 17	. 17 ¹
72. Reserve for housing corporation, amortization.....	18, 625. 92	0	. 01
73. Reserve for bad debts.....	10, 325, 105. 30	. 59	. 61
74. Undivided profits.....	14, 859, 373. 12	. 84	. 69 ¹
75. Surplus fund ¹	123, 934, 830. 20	7. 03	6. 97
76. Total.....	1, 763, 083, 070. 08	100. 00	100. 00 ¹

¹ Table is as follows:

	Percent to total assets	
	June 30, 1959	June 30, 1958
Surplus fund to due depositors.....	7. 89	7. 81
Surplus fund and undivided profits to due depositors.....	8. 84	8. 58 ¹
Surplus fund, undivided profits and reserves to due depositors.....	10. 08	10. 07 ¹

EXHIBIT III

BALANCE SHEETS REFLECTING ASSUMED BANK'S POSITION
BEFORE AND AFTER BOND TRANSACTIONS DESCRIBED IN
TEXT

CASE I

Before:

<i>Assets</i>		<i>Liabilities</i>	
Bonds.....	\$1, 000. 00	Due depositors.....	\$900. 00 ¹
		Net worth.....	100. 00
			1, 000. 00 ¹

NOTE.—Annual income, \$30.

After:

<i>Assets</i>		<i>Liabilities</i>	
Bonds.....	\$1, 000. 00	Due depositors.....	\$900. 00 ¹
Cash.....	39. 20	Net worth:	
	1, 039. 20	Beginning.....	100. 00 ¹
		Plus profit.....	39. 20 ¹
			139. 20
			1, 039. 20 ¹

NOTE.—Annual income, \$30.

CASE II

Before:

<i>Assets</i>		<i>Liabilities</i>	
Bonds.....	\$1, 000. 00	Due depositors.....	\$900. 00
		Net worth.....	100. 00
			1, 000. 00

NOTE.—Annual income, \$30.

EXHIBIT III—Continued

After:				
	<i>Assets</i>		<i>Liabilities</i>	
Bonds.....		\$832. 70	Due depositors.....	\$900. 00
Cash.....		95. 70		
		928. 40	Net worth:	
			Beginning.....	100. 00
			Less losses.....	71. 60
				28. 40
				928. 40

NOTE.—Annual income, \$35.39.

EXHIBIT IV

Summary—Bond income, profits and losses, 1946–58

(As percent of average investment)

Year	Operating income (1)	Net profit or loss (2)	Net income (3)
1946.....	2.49	2.28	4.77
1947.....	2.53	1.28	2.25
1948.....	2.54	1.61	1.93
1949.....	2.61	.35	2.96
1950.....	2.49	.11	2.60
1951.....	2.28	1.47	1.81
1952.....	2.47	1.17	1.30
1953.....	2.62	1.46	1.16
1954.....	2.68	1.97	1.71
1955.....	2.79	1.16	2.63
1956.....	2.97	1.55	2.42
1957.....	3.25	1.01	2.24
1958.....	3.50	.06	3.56
Average 1946–58.....	2.71	1.28	2.43

¹ Loss.

The CHAIRMAN. I have one general question I should like to ask.

I take it, then, that you support Mr. Martin's policy of having the Fed deal in bills only?

Mr. OHLENBUSCH. Mr. Chairman, I do not support the policy of dealing in bills only. I do not think that that is the Fed's position.

The CHAIRMAN. Virtually dealing in bills only?

Mr. OHLENBUSCH. I think there are appropriate times in which the Fed might operate in securities other than bills.

The CHAIRMAN. But these are exceptional?

Mr. OHLENBUSCH. I think these could be the exception rather than the general rule; yes.

The CHAIRMAN. Somewhere in your paper you said you seemed to favor dealing almost exclusively in bills only because you felt that if the Fed dealt in bonds of 5 years and more duration, this would affect the long-term interest rate. Is that correct?

Mr. OHLENBUSCH. Again, Mr. Chairman, I think it would depend entirely upon the conditions existing in the market at the time.

The CHAIRMAN. Did you not somewhere in your paper say that you did not want the Fed to deal in long-term securities because you did not feel it should influence the long-term interest rate?

Mr. OHLENBUSCH. That is correct.

The CHAIRMAN. I thought so.

Mr. OHLENBUSCH. I think, generally speaking, that is true.

The CHAIRMAN. I understand.

If it deals in bills, notes, and certificates, does it not affect the short-term interest rate?

Mr. OHLENBUSCH. I believe it has an influence; yes; by changing the quantity of money.

The CHAIRMAN. In a book of synonyms, "influence" and "effect" would be closely similar terms.

Mr. OHLENBUSCH. Yes.

The CHAIRMAN. Why is it all right for the Fed to effect the short-run interest rate?

Mr. OHLENBUSCH. Because I think the frequency of the problems as to whether or not an influencing of the rates is in order will be much greater in the short-term area than in the long-term area.

The CHAIRMAN. Yes; but if it constantly deals with short-terms, bills, notes, and certificates, it will constantly affect the short-term interest rate.

Mr. OHLENBUSCH. It cannot help but do that; yes.

The CHAIRMAN. And yet you seem to think that is all right, but it should not affect the long-term interest rate.

Mr. OHLENBUSCH. It affects the long-term rate indirectly, not directly.

The CHAIRMAN. Yes; but it affects the short-term rate directly?

Mr. OHLENBUSCH. Yes, sir.

The CHAIRMAN. You are saying that it is all right for the Fed to affect the long-term rate indirectly but not to affect it directly. Why is it proper to affect it indirectly but not directly?

Mr. OHLENBUSCH. I think that the long-term rate is affected by the actions of many, many individuals, and I do not think that this should be interfered with unless circumstances warrant direct action in this area. This is a part of the normal functioning of the market.

The CHAIRMAN. But what you say now is that the Fed, by dealing in bills, affects the short-term interest rate, and that this has an indirect effect on the long-term rate.

Are you as much of a purist as you believe yourself to be, then, in saying that the Fed should not affect the long-term interest rate when, by your own statement, it does so, only does so indirectly?

Mr. OHLENBUSCH. I think there is a difference, Mr. Chairman. As a matter of fact I now recall there is, or was at one time, provision for the Treasury to borrow directly from the Fed for short periods.

The CHAIRMAN. It is hard for me to see it.

Of course, as we all know, the relationship between the short-term rate and the long-term rate is not close and immediate.

Mr. OHLENBUSCH. That is correct.

The CHAIRMAN. During the depression, from 1929 to 1933, as I remember it, the short-term rate fell almost to nothing, but long-term rates were very slow in falling.

Mr. OHLENBUSCH. Yes.

The CHAIRMAN. In the recession of 1957-58, which I watched rather closely, the short-term interest rate fell, but there was not a very great movement in the long-term interest rate.

Mr. OHLENBUSCH. That is right.

The CHAIRMAN. So the long-term interest rate is somewhat lethargic in following the short term.

You know, sometimes the Fed argues the best way to control the long-term interest rate is through the short-term interest rate. Then they will say "well, we do not believe in controlling the long-term interest rate at all."

Perhaps I should take this matter up when I deal with the Fed, but since you are becoming a voluntary knight of the Fed, so to speak, k-n-i-g-h-t, I would like to say that at times I think the Fed is like the character in one of Stephen Leacock's stories who mounted his horse and rode off in all directions.

Mr. KLAMAN. Senator, this subject of the relationship between long- and short-term rates is of great interest.

I think you will agree that in the 1957-58 period to which you refer the operations of the Federal Reserve in the money market had a profound influence on the capital market as well, as reflected in the shifts of long-term investors among the alternative securities available.

The CHAIRMAN. I will read from Economic Indicators of July 1959, page 29, where the average rate on 3-month Treasury bills for 1957 as 3.267 percent falling to 0.81 percent in July of 1958, or a rate that is just about one-quarter of what it was before; but taxable bonds, of 5 years' and more duration, I assume Federal bonds, fell only to 3.20, a decrease of 27 points, or about 8 percent.

So one fell 75 percent and the other fell 8 percent.

Mr. KLAMAN. That is perfectly true.

One of the curves that unfortunately cannot be shown on this chart because of the lack of data is the curve for mortgage rates. Particularly in reference to the period after early 1957, the rise in the bond rate, which accompanied the rise in the bill rate, resulted in a very substantial shift on the part of long-term investors out of mortgages into corporates. Data on mortgage rates are unfortunately not as readily available as are the data on other types of interest rates. That is one of the areas that the Subcommittee on Economic Statistics should investigate carefully, I think.

The CHAIRMAN. If you take corporates, AAA's, the average yield was 3.89 in June of 1958, a fall of only 22 points, or only about 6 percent, at a time when the 3-month rate had fallen as we have said by almost 75 percent, or one-quarter of what it was. So on a geometrical scale the difference would be still greater.

Then, if I may pile up inferences, if you will notice the ballooning of the short-term rate since then, going back to July 18 to 3.401 on 3-month Treasury bills, the bonds rising to 4.08, as short-term rates quadrupled, the increase in the long-term rate was from 3.20 to 4.008, which is 88, or approximately 27 percent, compared to the increase of 300 percent in the other.

So when the Fed says that they will control the long-term rate through the short-term interest rate, it seems to me that this is very incorrect, and perhaps this is why you may favor affecting the short-term rate but not the long-term rate.

Mr. KLAMAN. Senator, I do not mean to suggest that the rate of movement in either direction will be the same. Clearly, the chart indicates this is not the case, but the direction of movement is very similar. You need only look at the record of net capital market flows from investors. Shifts were very marked in the 1957-58 period, much more than I had seen in most previous years. As a result of the

change in direction of interest rates, the savings banks went out of mortgages very rapidly in 1957 and early 1958 and into corporates.

Life insurance companies followed this pattern, with some lag, reflecting the difficult techniques of operating in the capital market. But the changed interest rate structure was very significantly reflected in the investment activity of financial institutions.

I am looking at the chart you have reference to, and I see that the movement between short- and long-term rates is fairly close during 1957. As a matter of fact, the movement is fairly close during the period from the beginning of 1956 through 1957. This is true of AAA corporates, Treasury bills, and other securities. And it does not require much of a movement in the long-term interest rate area to get investors to shift investments.

The CHAIRMAN. I think you can make much better case for saying that the shifts in yields of corporate bonds correspond much more closely to the shifts in yields on Government bonds than to say that they correspond to the yield on 3-month Treasury bonds.

Therefore, I have always felt that the fundamental rate was the long-term rate rather than the short-term rate, though I know a lot of experts attached to the Federal Reserve still say that the way to affect matters is indirectly through the short-term rate.

But this seems to be identical. If you compare the chart of movement of yield on taxable Government bonds with yields on corporate AAA bonds, you find the correspondence is very close between those and the 3-month rate. Is that not true?

Mr. KLAMAN. That is right.

The CHAIRMAN. This is really my quarrel with the Federal Reserve and not with you. But as I say, since you seem to be a voluntary defender of the Federal Reserve and move in financial circles, I thought I should bring that out.

Mr. Frucht here represents the minority, and since there are no representatives of the minority present, I think he should be privileged to ask a question directly.

Mr. FRUCHT. On this question of substitution as between the long-term and the short-term market and the relative change in the short-term rate and the long-term rate, I wonder if the major variable in this relationship is not the change in the maturities of the debt. In other words, there is another adjustment mechanism apart from the changes in the rate. In other words, if during this period there was not a drastic shortening-up in the maturity pattern of the Government debt as another variable of adjustment.

Mr. OHLENBUSCH. I do not think there has been much change in the maturity pattern of the Treasury's debt within the time you spoke of. Would you say so, Mr. Chairman?

The CHAIRMAN. I do not know. The period which you spoke of was a relatively short period, from 1957 until June of 1958, really a period of less than a year. Then the next period was a period of a year, approximately.

Mr. OHLENBUSCH. I think it probably was a very small, possibly even insignificant factor.

The CHAIRMAN. There is a downward drift, of course, in the length of maturities. But whether there has been a rapid shift I do not know. You probably have the figures there.

If I may return to your own problems. Your statement seems to indicate that you hold about \$200 million in Government bonds.

Mr. OHLENBUSCH. That is correct, yes, sir.

The CHAIRMAN. With this as an average on the amount existing at any one time, what would be your total volume of purchases and sales of Governments within the year? These are your holdings at one time.

Mr. OHLENBUSCH. The total purchases and sales?

The CHAIRMAN. In other words, would you hold these relatively constant or would you be in and out of the market quite directly?

Mr. OHLENBUSCH. We would not hold these very constantly, but on the other hand we would not be in and out of the market with great frequency, either.

The CHAIRMAN. The tests of this would be the total volume of purchases and sales as compared to the average holdings? This would give one the rate of turnover, so to speak, in the Government securities.

Mr. OHLENBUSCH. Yes. The rate of turnover, I think, in all probability would be of the magnitude of one. In other words, the total purchases might amount to \$200 million and total sales \$200 million. But it could very well be that on no single day was there less than \$200 million invested in Government securities.

The CHAIRMAN. You have never computed these figures?

Mr. OHLENBUSCH. I do not recall them. We have the records at the bank.

The CHAIRMAN. Would it be too much work to compute them for the record at this point?

Mr. OHLENBUSCH. No, indeed. Certainly.

The CHAIRMAN. But your offhand judgment is that it is a turnover rate of probably one?

Mr. OHLENBUSCH. Yes, probably something in excess of one.

(The material referred to follows:)

(See letter, p. 1449.)

The CHAIRMAN. Who decides how much of the bank's assets will be in mortgages, how much in bonds and so on? Is this done by the trustees?

Mr. OHLENBUSCH. Yes, by the trustees.

The CHAIRMAN. They make that decision.

And do you determine what Government securities will be purchased, or do the trustees determine this?

Mr. OHLENBUSCH. The trustees determine it, within a general framework of overall maturity, as to which specific issues we may be in today as opposed to next week.

The CHAIRMAN. They determine the general policy and you implement that policy in determinations of specific choices?

Mr. OHLENBUSCH. Precisely.

The CHAIRMAN. Can you make large purchases without approval of the officials?

Mr. OHLENBUSCH. Yes, indeed, unlimited purchases and sales.

The CHAIRMAN. Without the approval of the trustees? Without their prior approval.

Do you do this very often?

Mr. OHLENBUSCH. We do this fairly frequently. We just went through such an example here within the last week, when we sold

approximately \$25 million of Treasury notes and bonds maturing in 1963, 1964, and 1965, to purchase the new Treasury offering due in 1964.

The CHAIRMAN. When you carry out these purchases of Government securities, how do you get them?

Mr. OHLENBUSCH. This is done through the Government bond dealers who operate in this field.

The CHAIRMAN. The 17 security dealers?

Mr. OHLENBUSCH. That is correct; yes.

The CHAIRMAN. Then, on new issues, do you buy directly from the Treasury or buy through the bond dealers?

Mr. OHLENBUSCH. That would all depend upon the particular issue. For instance, in the offering that the Treasury made here about a month or so ago of July 15, 1960, discount bills, it obviously would have been foolish for us to subscribe directly, because we do not get the advantage inherent in the tax and loan account. There we would wait and buy from dealers in the secondary market, as we refer to it, as opposed to the new issue.

With respect to this rather large transaction I speak of that we just went through, we purchased rights, and then we convert those rights through the Federal acting on behalf of the Treasury.

Have I answered your question?

The CHAIRMAN. Yes, I think so.

When you do make your purchases from dealers, is there any particular set of dealers with whom you primarily deal, or do you place your orders across the board, more or less?

Mr. OHLENBUSCH. On a given transaction, we would place all of that transaction with one dealer. In other words, we would not have a number of dealers operating in precisely the same situation all competing with each other in our behalf.

The CHAIRMAN. I understand. Certainly.

But in successive issues, do you deal across the board with a wide number of dealers or primarily with a few, or with one, or what?

Mr. OHLENBUSCH. I would say that most of our dealings were done with about six or eight of the dealers. I did not include the banks. I should have included banks. There would be another two banks.

The CHAIRMAN. You mean among the security dealers?

Mr. OHLENBUSCH. Yes. Among the total of 17 I would say we do business with approximately 10 to 12.

The CHAIRMAN. Is there any one dealer with whom you do most of your business?

Mr. OHLENBUSCH. I would say that we have a pretty good distribution of our business among these dealers.

The CHAIRMAN. And there is no one dealer with whom you do most of your business?

Mr. OHLENBUSCH. I would say not; no.

The CHAIRMAN. Would it be too much trouble to furnish for the record an account of the various amounts which you have bought and sold through the various dealers?

Mr. OHLENBUSCH. Over what period, Senator?

The CHAIRMAN. Over last year, say.

Mr. OHLENBUSCH. Over the last year? I would rather do it over a little longer period, if you would have no objection to that.

The CHAIRMAN. Could you segregate the last year? And then if you want to take on any extra work, you may provide that.

Mr. OHLENBUSCH. We would be very happy to do it that way. (See letter, p. 1449.)

The CHAIRMAN. I suppose everyone is trying to guess what the Federal Reserve is likely to do.

Mr. OHLENBUSCH. I would say interested, surely. Of course, we are interested. We are trying to guess. I would say, though, that I do not think it is a major element, a major determinant in our investment policies.

The CHAIRMAN. You do not think it is much of an influence?

Mr. OHLENBUSCH. I do not think it has a great deal of bearing on our investment policies. True, at times it will have some. But at this particular moment I do not think it does.

The CHAIRMAN. Is this based on the assumption that the Federal action does not affect, after all, the long-term interest rate, in which most of your investments are made?

Mr. OHLENBUSCH. No, Mr. Chairman; as I regard our job, it is to invest in long-term obligations to the best advantage that we can at the time that we receive the money. We will try to eke out a little advantage by shifting around at times from one group of long-term investments to another, according to the ebb and flow of funds as I have described in my prepared statement.

The CHAIRMAN. But do you think that the action of the Reserve has an influence, either cyclical, direct, or indirect, upon the long-term interest rate? If so, the expected action of the Reserve becomes very important; is that not true?

Mr. OHLENBUSCH. Yes.

The CHAIRMAN. How do you estimate what the Reserve is going to do? I have often wondered about this, as to the relative mindreaders in New York and elsewhere.

Mr. OHLENBUSCH. This will have a great bearing on the level at which we invest our money, but we do not try to out guess, as it were, the Federal Reserve and base our investment decisions on what we think the Federal Reserve is going to be doing.

The CHAIRMAN. I have noticed that these government issues are always oversubscribed. You have noticed that, too, have you not?

Mr. OHLENBUSCH. We have, indeed.

The CHAIRMAN. How do you account for this?

Mr. OHLENBUSCH. I think fundamentally it is the manner in which the Treasury must make its offerings of securities to all comers. I think rather an undesirable situation was created when the Treasury gave preferential allotments to certain types of investors. I think this is rather an undesirable, undemocratic sort of thing. I believe the Secretary of the Treasury pointed out to you that for a new borrower to sell his securities in the market, he must offer them at a rate a little bit better than the rest of the market, to induce investment in his new offering as opposed to all of the outstanding offerings and securities.

This creates a little element of profit. This brings in people who might not otherwise be brought into an offering of this sort. I think at times, and I do not think this is a desirable thing at all, it will bring them in a speculative position in the sense that they are using

borrowed funds to do this kind of thing; and I think I would differentiate here between a Government dealer borrowing funds to make the subscriptions and an individual or corporation borrowing money for this purpose.

The CHAIRMAN. Have you found that in order, let us say, to get a million dollars' worth of a new issue, you have to ask for more than a million dollars' worth?

Mr. OHLENBUSCH. Yes; indeed.

The CHAIRMAN. Is there any ratio generally that you have to have of the number of millions of dollars that you will have to bid for or subscribe for in order to get a million?

Mr. OHLENBUSCH. This will vary from time to time, Mr. Chairman. As you know, there have been times in the past when you have had to oversubscribe to the magnitude of maybe five times what you hoped to get.

The CHAIRMAN. But how do you know the ratio that you will apply? Five times or three times or twice or one time, or 10 or what?

Mr. OHLENBUSCH. Believe me, this is one of the things I do not like to do. I feel very uncertain, having made a subscription of this kind. I wish you and the Treasury and its other advisers could find a solution to this problem.

Of course, the way we do it is this. We all talk to each other, we talk to all of the dealers, the dealers talk to all the other investors.

The CHAIRMAN. Will they have lunch with them?

Mr. OHLENBUSCH. It will be done by telephone. And we try to appraise the situation as to whether allotments will run 20 or 70 percent, as the case might be.

The CHAIRMAN. In other words, you find out what the other boys are going to do, and do likewise.

Mr. OHLENBUSCH. That is about the way it works. It is a most undesirable situation. I rest most uncomfortably for those few nights when I do not know whether we are going to get a 10-percent allotment or a 100-percent allotment on these cash offerings.

The CHAIRMAN. Have you studied the suggestion which some of us have made, which might reduce your headaches and worries and permit you to sleep more quietly and pleasantly in your suburban home; namely, that these issues be sold under the auction system?

Mr. OHLENBUSCH. Yes; I have.

The CHAIRMAN. You would not have to worry as much then, would you? You might have to worry about the amounts you would bid, but not so much about the quantity for which you would subscribe; is that not true?

Mr. OHLENBUSCH. I would have to be deeply concerned about the price at which I had made my bid; that is right.

The CHAIRMAN. But you would not have to worry about the multiple?

Mr. OHLENBUSCH. No, I would not; that is right.

The CHAIRMAN. Is there any possibility of making a convert of you to this proposal that bonds be sold under the auction system? We made converts among the life insurance companies yesterday.

Mr. OHLENBUSCH. You did?

The CHAIRMAN. Yes; indeed. They were even willing to disagree with the Treasury and the Federal Reserve on this point, which sur-

prised me. I want to see if this united front which is generally presented to us by the financial interests of the country can include the mutual savings banks as well.

Mr. OHLENBUSCH. If you had asked me that question, Mr. Chairman, from the standpoint of my own personal feelings, I would rest much more comfortably under such a circumstance as you have suggested. But I am also mindful of the fact that the Treasury should be served in this matter, too. I think that here we have a little different story. I think if I were looking at this from the standpoint of the Treasury, I would find otherwise. I think it would be a most undesirable thing for the Treasury.

Obviously, this suggestion stems from the fact that the Treasury each week so successfully sells its bills by this method. I assume you are talking about the auction method here. In the case of bills you are dealing with a relatively small group of very sophisticated professional investors. They are all very keenly in touch with their market. They know in most instances to within a few one-hundredths of 1 percent where these bills are going to sell. If they miss by 1 or 2 basis points, even as much as 10, this is relatively insignificant. Surely, they will have taken a little loss if they bid a price 10 basis points too high. If your bid is off 10 basis points in a 40-year bond, however, you have exposed yourself to a loss in excess of 2 points, and this is a major difference.

I think I would rather take the risk of getting a smaller allotment under the Treasury's present procedure of offering at fixed prices than I would of placing the Treasury in the position of getting this very, very wide spread that it might receive on bids for long-term bonds.

The CHAIRMAN. Of course, you realize the auction system which some of us have been proposing differs from the competitive bidding system on public utilities and municipals, where the entire issue will be taken at a given price, and the one who makes the best bid for the whole issue, or the syndicate which makes the best bid for the whole issue will take the whole issue.

Mr. OHLENBUSCH. Yes, indeed.

The CHAIRMAN. But under the auction system, with each one quoting a separate price, then the quantities are disposed of to the buyers at the prices which they designate.

Would this not have the advantage to the Treasury that you would, instead of selling all perhaps at the lowest point at which the market would move, it would be able to get the bids in excess of this amount, and therefore the net return to the Government would be greater than it is presently?

In other words, you could skim off some of the surplus which now goes to the dealers.

Mr. OHLENBUSCH. To be sure, you would accept only the highest bids.

The CHAIRMAN. But you would accept a variety of bids.

Mr. OHLENBUSCH. But you would exclude the lowest ones.

The CHAIRMAN. Certainly. But it would not all go to the highest bidder.

Mr. OHLENBUSCH. No. No; I understand. It would be done precisely as bills are sold each week now.

The CHAIRMAN. That is right, only with a broader market. It is not proposed that only 17 dealers could handle these. You could come in directly without operating through a dealer.

Mr. OHLENBUSCH. Yes.

The CHAIRMAN. The life insurance companies could do similarly. Informal syndicates could be formed.

Mr. OHLENBUSCH. Yes.

Each week in the bill bidding, Mr. Chairman, you have the dealers submitting what they call throwaway bids. You are familiar with the fact that each week's offering of bills is very heavily oversubscribed. But if you note the oversubscription, it is usually at a very much lower price.

We must bear in mind that if the Treasury were to offer long-term bonds on the basis that you have suggested, you are dealing with an entirely different group. You are dealing with an unsophisticated group of investors. You are dealing with something which cannot be pinpointed as finely as can the yield on Treasury bills. You would have the large investors putting in, as they say, "throwaway bids," bids which they do not think will be accepted, but they will put them in there to go along with the Treasury. Large investors will not want to be exposed to this matter of having paid substantially above the average price to get the bonds.

We are not as skilled in this field. The long-term field is not subject to the same precise degree of measurement as is the short-term market. I think it would serve the Treasury poorly, were it to institute such a procedure.

The CHAIRMAN. But you think it is a subject that should be considered very carefully?

Mr. OHLENBUSCH. I do, indeed. Yes, sir.

The CHAIRMAN. You know the Treasury and the Reserve brush this off very cursorily, and in their three-volume study, so far as I can ascertain, they are completely confused as to what we are proposing. They seem to think—and I will ask the staff to check me on this—that what those of us who advocate an auction system are proposing is that the auction system should be used for already existing Government securities. This is not the point at all. What we have been proposing is that the auction system be used on the issuance of new securities. And I want the record to show that very, very clearly.

I think the Treasury and the Reserve have been setting up a man of straw, so to speak, and knocking down this man of straw and not dealing with the real issue.

Mr. OHLENBUSCH. I certainly think it is well worth investigating, Mr. Chairman. But my offhand opinion is that it would not work to the Treasury's advantage.

The CHAIRMAN. Thank you very much.

Vice Chairman Patman is going to take over now. I hope you will forgive me for leaving, but I have to go on to another committee meeting. But you are in good and sympathetic hands here with Congressman Patman.

Representative PATMAN. I was very much interested in what you had to say about oversubscription being necessary.

Mr. OHLENBUSCH. It becomes very difficult at times to convince unknowing trustees that this kind of thing is necessary.

Representative PATMAN. The advisory committees of the Treasury, when they go around and find out about what the interest rates should be, and when they call people like yourselves in to confer with to determine what interest rates should be put on an issue, do the people who are contacted not invariably keep low the amount they will probably subscribe for? And then, when they go to subscribe, they subscribe about five times that much in proportion to what others subscribe?

Mr. OHLENBUSCH. I do not know the answer to that, Mr. Patman. I would have no way of knowing. I am on one of these groups you mention—one of these advisory groups. I have heard the statements made by individual members of this group that our interest would be so-and-so many millions or thousands of dollars, as the case might be. I have no way of knowing whether this was an underestimate or an overestimate. I can assure you, however, that with us it was an honest estimate.

Representative PATMAN. Of course, I am not accusing anyone of making a dishonest estimate. But when they are being contacted about the probable rate of interest, if they indicate that the amount they will subscribe for is much less than what they are actually going to subscribe for, that has a tendency to keep the interest rates higher, does it not, rather than lower?

Mr. OHLENBUSCH. I think, Mr. Patman, that we would be hopeful of getting this quantity of bonds. It may develop that a subscription of twice this amount is necessary; it may be that a subscription of five times this amount is necessary to achieve that goal.

Representative PATMAN. In the sale of Government securities, I know it has been a traditional practice to sell them in the open market. I know that the law requires, so far as the Federal Reserve is concerned, to buy in the open market. Therefore, the Treasury must sell in the open market in order for the Federal Reserve to buy in the open market.

But is there a law compelling the Treasury to sell all securities in the open market?

Mr. OHLENBUSCH. I am sorry, Mr. Chairman, I would not know the answer to that.

Representative PATMAN. But it is always done that way, is it not?

Mr. OHLENBUSCH. Yes.

Representative PATMAN. If the law requires the sale of all securities in the open market, do you not think we should consider whether or not that law should be changed to permit negotiated sales, possibly, and permit the Federal Reserve to buy under certain circumstances directly from the Treasury and not have to go through these 17 dealers?

Mr. OHLENBUSCH. I do not see what we could hope to achieve by this, Mr. Chairman.

Representative PATMAN. As it is now, you used the phrase "a small group of sophisticated investors." You meant the 17 dealers, did you not?

Mr. OHLENBUSCH. I meant the 17 dealers, including the dealer banks; but in addition to that, a great many banks which are not dealers.

Representative PATMAN. I know, but that could be a bottleneck in some cases.

Mr. OHLENBUSCH. Indeed, it could.

Representative PATMAN. And it could react against the interests of the Treasury.

Should it not be possible under certain conditions for the Treasury to negotiate sales and under other conditions to sell them just directly to the Federal Reserve banks where necessary.

I think during World War II practically all the short-term issues were sold to the Federal Reserve through these dealers. But the question is, Why, when the Federal Reserve has to buy an issue, should the Federal Reserve have to buy it through the dealers? Why could they not buy directly?

Mr. OHLENBUSCH. I have not given this matter any thought. I can see no disadvantage to it as a temporary measure.

When the Federal Reserve buys or sells short-term securities, it does so to affect the quantity of credit outstanding. It may even, for temporary periods, do this to assist the Treasury marketing operations.

These holdings will go up or down with credit requirements. However, the amendment we are talking about calls for assistance to the Treasury in its debt management problems by purchasing longer maturities. I think therein lies the difference.

Representative PATMAN. Do you see any disadvantages that accrue to the Treasury in any case where they have to deal with these 17 "sophisticated investors," as you call them? In other words, should it be opened wider and more dealers be permitted?

Mr. OHLENBUSCH. As Mr. Klamann just prompts me, there is no limitation on the number of dealers. I think it is a matter that anyone can become a dealer who has the wherewithall, both money and brains, to do this kind of thing.

Representative PATMAN. That sounds good; yes, sir. At one time they did have an exclusive list, as you know, and I think our investigation before this committee had something to do with breaking it up. At the same time, I think the rules and requirements would necessarily restrict it to a few dealers.

Anyway, there are only 17 dealers in the United States. That, of itself would cause just a little curiosity.

Mr. OHLENBUSCH. Yes.

Representative PATMAN. But we will not go into that, because we are not familiar with it, and I am sure I am not either, about the absolute requirements.

I noticed in your assets here you made a lot of loans to banks. I was amazed to find out that banks like the Bank of New York, the Bankers Trust Co., and the Chase Manhattan Bank, the Chemical Bank, and all those big banks were borrowing money from your institution.

Mr. OHLENBUSCH. These are not borrowings. These are our deposits.

Representative PATMAN. They are deposits by the banks?

Mr. OHLENBUSCH. By the Bowery Savings Bank.

Representative PATMAN. With your bank?

Mr. KLAMANN. No, the reverse. Deposits by the Bowery in these commercial banks.

Representative PATMAN. Oh, you have made deposits in these commercial banks?

Mr. OHLENBUSCH. Yes.

Representative PATMAN. I see. That explains it.

I am anxious to ask you about shopping centers. I understand that your group and possibly your own great concern makes loans to shopping centers over the country. As chairman of the Small Business Committee of the House, I have lots of complaints from small-business people. One of them has been that local grocerymen or druggists, local small businessmen, are unable to get into these shopping centers; that someone will come to town and say he is going to build a big shopping center, and the local people will say, "Well, I would like to be in the shopping center, I would like to get space, rent space," and they are not able to negotiate a deal with the people who are building the shopping center. They are invariably told—whether it is true or not, I do not know; I am just asking you—that they cannot get in, because they prefer to deal with national chains because they have more security in dealing with people that have a large number of outlets, like interstate chains, and they have greater security that way.

I can see a good reason for it from strictly a standpoint of solvency and security. But it occurs to me that the local people, if they are correct about this, have a point there, that it means ultimately that outside owners will own the businesses in the local community.

In my book, that is bad. I think that a local business that can be conducted by local people and owned by local people is always the best.

Of course, we must have big business, we know that; and we must have businesses not conducted locally, we know that. But with a business that can be conducted by local people, local people should be encouraged to own the business.

If their complaints are correct about these shopping centers, that has a tendency to displace the local man and install an outsider in the local enterprises there. What is your answer to that?

Mr. OHLENBUSCH. First of all, I want to qualify my answer to that question by saying I am not the bank's mortgage officer. You know Mr. Held, I believe, who is our mortgage officer. I do sit on the bank's mortgage committee, so I have been in on many of the discussions on problems of the type that you are discussing here.

We regard this matter of what we would call major tenants in a shopping center in this way: We would want to see enough income from high credit standing tenants in a given shopping center to provide for the payment of the taxes, the interest, and the amortization. I do not think we would necessarily say that these have to be national chains. If a local merchant can present to us a statement showing that he is as good a credit as a national chain, he will be just as acceptable as a national chain would be.

Representative PATMAN. It would be very difficult for him to do that, though, would it not? I happen to know one in a Midwestern State who is well fixed, worth a lot of money. He offered to put up any amount of money that they required to get his drugstore in this shopping center, and he was turned down.

Mr. OHLENBUSCH. I think, Mr. Patman, that if that is the case, it is rather a sad reflection on our investment industry in the United States. I can assure you that with us, a small store with a high credit

rating will get as much consideration as will a national chain with a similar credit rating. This is not a matter of size. This is a matter of proportions.

Mr. KLAMAN. May I add a point to that, Mr. Patman?

Representative PATMAN. Yes, sir.

Mr. KLAMAN. Fundamentally, industrywide, the financing of shopping centers and other business enterprises is handled in the main by commercial banks and life insurance companies. Savings banks are more largely in the residential financing area, including rental housing as well as owner-occupied housing. To the extent that there are shopping centers involved, in large part the sponsors of the centers—this is, of course, a very specialized area, and there are a lot of specialists involved here—will determine how occupancy shall be meted out, having once arranged for the major tenants. You see these shopping centers everywhere, and usually you have two large stores, one on each side of the center. This is typical, for the traffic pattern. They have a Garfinckel's and a Woodie's on the left and right, and in between these small stores.

Typically, in this Washington area, which is a very good example of the development of shopping centers, most of the small stores are locally owned. If you look at any one of these centers, you see several small stores buttressed on each side by the major department stores or by food chains.

Once the builder or sponsor obtains his loan commitment the builder has obtained that, he can get his construction financing from the commercial bank, and he is ready to go ahead with his shopping center.

He in large part will determine who else should come into the center to make it a success. It is not entirely in the hands of the financial institutions. By this I mean the commercial banks and life insurance companies, much more than savings banks, as an industry-wide matter in terms of the kind of financing that we do.

Representative PATMAN. I believe you told me in conversation before the meeting was called to order that you tried to have at least two-thirds, which seems to be a very reasonable amount, tied down in long-term leases which would guarantee you your interest and your payments, and so forth.

Mr. OHLENBUSCH. Mr. Chairman, I do not know what the precise ratio would be. I think the important thing would be that we would like to see what we call the nut covered by tenants with high credit standing. It may be two-thirds, it may be three-quarters, it may be 80 percent of the project's total income.

Representative PATMAN. Of course, the chains can offer long-term leases, and the individual cannot very well do that. Besides, you would be taking a greater risk with an individual than you would with a corporation like a national chain.

Mr. OHLENBUSCH. No, I am afraid I cannot agree with that.

Representative PATMAN. You do not agree with that?

Mr. OHLENBUSCH. Not at all. We have many loans, not on shopping centers, but on factories, where we have just a single credit involved, where it will be a small and local industry. But if that occupant, if the owner has a high credit rating, he gets his money just the same as any other larger organization would with a similar credit standing.

Representative PATMAN. I am not charging there is any intent on the part of investors to discriminate against local people, but I can see where in some instances it would result in that, because some of them are not qualified, of course; and local people cannot get the money, and large concerns can get it, because they are in a better position to get it. And sometimes it works a great hardship on local communities, I am afraid.

I think one of our greatest economic problems probably is right there in the local ownership of local businesses versus the absentee ownership of business. A lot of our towns and communities are drying up over the Nation. It is really pitiful. Then, we have a lot of chronic unemployment areas, distressed areas, and I am afraid we are going to have more of them. It is a serious situation.

I know it is not the intent of the investors to cause or to aggravate a situation like that at all, and I am not charging it. But I certainly hope that something is done to reverse this trend. There is too much of it that way, I think.

Mr. OHLENBUSCH. Mr. Patman, may I point out one of the difficulties here that surrounds this matter. When you are dealing with a large chain and you ask that large chain, "We want to see your financial statement," they have experts in this field, and they know precisely what we are asking for. They are ready to give us just exactly the information that we are looking for and we need to make a proper appraisal. This is most difficult with a small corporation.

Representative PATMAN. I know it is.

Mr. OHLENBUSCH. You just have to dig and dig and dig. You have to call them on the telephone and ask, "What is the answer to this? What is the answer to that?"

Representative PATMAN. That is the reason I could not blame an investor or people like you for dealing with a large chain. They can furnish you the information you need quickly, they know what the score is, and can be helpful to you, and why should you deal with individuals and have to train them, educate them on these things?

Mr. OHLENBUSCH. It is not a matter of educating them. It is a matter of our costs in, in a sense, developing this information which we need before we can make such a loan.

Representative PATMAN. That is right. In the Defense Department, I hope it is not so bad now, but at one time I was impressed when they were letting contracts. They let the contracts to the big concerns that, as you say, had the experts, had the know-how, had everything, and why should this contracting officer run the risk of dealing with some little fellow who did not know and who would probably fall down on the job, or possibly do so, when he could deal with the large concern and not be criticized for it? For that reason, many large concerns got a disproportionate amount of the business. But you could hardly blame the procurement officer, because he was acting in good faith and wanted the job done right.

Mr. Coffin, do you want to ask some questions?

Representative COFFIN. Yes, I do.

Representative PATMAN. I would be glad to yield to you, sir.

Representative COFFIN. I am sorry I came in late and did not have a chance to hear your testimony.

I wonder if either of you gentlemen could tell me whether or not you participate on the Advisory Committee which consults with the Treasury prior to issues?

Mr. KLAMAN. We do.

Mr. OHLENBUSCH. I am a member of such a committee, and Mr. Klamán is economic adviser to that committee.

Representative COFFIN. Are you the economic adviser?

Mr. KLAMAN. Well, Mr. Coffin, we operate through the National Association of Mutual Savings Banks. I am director of research for the association. Mr. Ohlenbusch is a member of our government securities committee. It is the government securities committee of the national association that is invited to Washington on occasion, not regularly, in connection with their new issues of refundings.

Representative COFFIN. Can you tell me how you, as a person not only on the committee but also with certain operational responsibilities, go about determining what the amount of total subscription might be to a particular issue concerning which you have a discussion?

Mr. KLAMAN. Actually, we do not determine this, Mr. Coffin. Upon occasion, the Secretary or his advisers will ask what we think the savings bank industry might subscribe for. On most occasions we pointedly indicate that we do not really know, we cannot tell, and we do not think that it is a good idea to survey the industry in advance as to what they will do in the event the Treasury makes the offering. This in itself would have some kind of an effect on the market.

So when we come to the Treasury, we simply come and offer our best judgment about the state of the market, what we think would be to the best interest of the Treasury in its offering, whether it is a refunding or a new offering, and what we think they would have to do in order to have a successful issue.

Representative COFFIN. When you make that sort of a response to the Treasury, you are not talking about the reaction of the other financial institutions to the proposed issue, but only of the savings banks?

Mr. KLAMAN. Certainly we know most about our own industry, and we indicate to the Treasury what we feel the market is like and what we think it would be necessary for them to do in order to get a favorable response to an issue.

Representative COFFIN. Is there a panel discussion or a group discussion when you do this?

Mr. KLAMAN. It is rather informal. For example, if you are interested in this procedure, I would by following the market try to determine what the state of the market was and whether it would be possible for the Treasury to sell a long issue or a short issue, and what rate would be necessary if it is a long issue outside of the bill area, in order to have a successful offering.

I would prepare a memorandum on this, just outline the market as I see it after talking to various responsible people. This memorandum would go to the various members of our committee as background information so they will be better informed about the market situation.

Then I might suggest in this memorandum, "it looks at this point as if the Treasury could do only one of two kinds of offerings." We would then meet in Washington ourselves and have some discus-

sion about what we thought would be the best recommendation, and we would prepare on most occasions a formal, written memorandum. We would sit around in the Treasury and discuss back and forth what the market is. They have presentations which they show us, on the state of the market and Treasury issues and so forth, which is very helpful, and then we present our suggestions.

Representative COFFIN. Is the focus on a specific issue coming up in the near future, or do you undertake to say what the issue should be?

Mr. KLAMAN. It is always in connection with an immediate offering or refunding. It is not in connection with Treasury policy over a long term.

Representative COFFIN. Do you not meet every time there is an offering or refunding?

Mr. KLAMAN. No. The commercial bankers and investment bankers do, mainly, but the long-term investors rotate. We meet once, the life insurance companies meet once, and so on.

Representative COFFIN. But these meetings are held only when long-term issues are contemplated; is that it?

Mr. KLAMAN. Not necessarily.

Mr. OHLENBUSCH. Usually each time the Treasury has an issue under consideration, either for refunding or for new money.

Representative COFFIN. Are you always called in when there is a long-term issue in prospect?

Mr. OHLENBUSCH. At one time the Treasury did do that, but then market observers interpreted our presence there as meaning that a long-term offering would be made, and of course this created an undesirable situation. Since then, as Mr. Klamman says, the Treasury has been rotating as between savings banks, savings and loan associations, and insurance companies.

Representative COFFIN. In your business, you must have various ways of making up your own mind what the market is at any given moment. This is your business. You have to keep on top of this all the time.

The other day, when Secretary Anderson was testifying, I asked him whether or not it would be possible to systematize the conveying of information about the market to the Treasury to a greater extent than they do now.

They, of course, are on top of the market all the time. But either in addition to use of the committee, or in substitution for it, probably in addition to it, as another tool, could they not have skilled people whose sole job it would be to go through the country and talk on an individual basis with people in key financial spots to get their reactions—not necessarily a group reaction, but an individual reaction, that would not be communicated to others, so that perhaps there might be a more accurate consensus even than that which comes out of the process which Mr. Klamman described?

Mr. OHLENBUSCH. I think, Mr. Coffin, in effect, the Treasury does something like what you are talking about, because in addition to interviews with these American Bankers Association and Investment Bankers Association committees that we have spoken about, the Treasury also will interview the dealers and representatives of major banks directly. How far they extend this, I do not know. I just know that from time to time they are in New York talking to Government

bond dealers individually, not as members of committees. They will talk to banks individually. Whether they would extend this to Chicago and to other large centers, I would not know.

Representative COFFIN. What I am talking about is a situation where you have a systematic survey from time to time so that you could compare the reaction one time to that of a previous time; that is, such a comprehensive survey so that you can say it represents at least 90 percent of the same people who were interrogated before, or at least a fair representation of the whole market, so that you might over a period of time be able not only to know what their thoughts were at the time, but to compare it with previous censuses.

It just seems to me that this most important marketing procedure should leave no stone unturned to take advantage of every tool that modern polling techniques and scientific statistical analysis make available.

Mr. OHLENBUSCH. I do not know precisely the manner in which the Treasury uses this information which they thus gather. I would be hopeful that they would keep a memorandum from time to time of their records in this area. I think it would be very useful to them.

Representative COFFIN. I have also in mind that from time to time, justly or unjustly, the committee comes under criticism because it is a fairly small group, although it represents a great part of the industry. But this would be a means also of making it quite clear that we were trying to get every bit of information that might be helpful on new issues.

Mr. OHLENBUSCH. Believe me, our committee comes under the criticism of our membership, too.

Representative COFFIN. That shows you have a healthy association.

Mr. OHLENBUSCH. We are not running a popularity poll.

Representative COFFIN. This is a different subject.

In the not too distant past; namely, in 1955-57, when we had rising long-term rates of interest, it was the opinion of many, if not of all, that this phenomenon had its greatest effect on the mortgage market, residential housing.

What my question seeks to determine is this: If the interest rate ceiling on Government bonds is raised and long-term rates rise still further, what would be the effect? Could we expect this effect, once again, to be concentrated on the mortgage market, residential construction, housing?

Mr. OHLENBUSCH. Again, this is a field in which I am not primarily qualified. I might just make a general observation, though.

I think that if we were to free, as it were, the rate on Government securities and keep fixed the rate on mortgages, mortgage investment would tend to suffer as rates went higher. There is no question about that. I think that would be true if we continued to keep the rate on Government bonds at 4¼ percent. We would just lose all our friends here.

Representative COFFIN. Then you think that if the rate on long-terms went up, the impact of higher rates would concentrate on residential construction?

Mr. OHLENBUSCH. In my judgment, this would happen in the period you are talking about just exactly as you have described.

Mr. KLAMAN. As Mr. Ohlenbusch mentioned, Mr. Coffin, this in large part is a reflection on the artificially fixed interest rates in the

mortgage market. The question is, is it desirable to have free market rates operative in the whole capital market area. Whether or not the ceiling is raised on long-term Governments, you are likely to find a severe pinch in the mortgage market. You already have it. It need not be related to the long break in the Government market, because obviously corporate rates are free to rise, borrowers there are very active in the market, and already there are signs of shifting out of the fixed interest rate area, for obvious reasons.

The question is, Does it make sense to free the rate in this large area of the mortgage market and permit borrowers to compete freely? It may well be that because of the structure of the market, mortgage borrowers would still not be able to compete as easy as some of the long-term corporate borrowers. But at least they would have the opportunity to compete. Right now they are not given that opportunity. It does them little good to know that up until recently a VA loan was available at $4\frac{3}{4}$ percent if no VA money was forthcoming.

It finds reflection in other ways. It finds reflection in prices of housing.

Representative COFFIN. Are you suggesting that we free-up all Government-guaranteed mortgage programs or direct loan programs?

Mr. KLAMAN. It is my view that this would be a very important part of permitting the mortgage market to rid itself of the violent swings that it has been subject to in the postwar period.

Representative COFFIN. It would permit it to rid itself of violent swings, but would we not see a very substantial upward trend?

Mr. KLAMAN. Well, this is a question of whether or not you believe that in most cases markets should be free to operate, reflecting the supply and demand forces; that it will be upward when the demand for funds is in excess of savings. The only really lasting way that you can prevent a long-term trend of rising interest rates is to encourage and increase the volume of savings. This is where the mortgage money comes from, fundamentally.

Representative COFFIN. I assume you have been interrogated already on what would have been the situation in June of 1958 had the Federal Government gone in for a time to purchase long-term bonds?

Mr. KLAMAN. Mr. Ohlenbusch commented on this in his statement, but we have not been questioned on it.

Representative COFFIN. Well, what would you say?

Mr. OHLENBUSCH. We volunteered a statement on that point.

Representative COFFIN. The question is, you had this widespread discrepancy between the long terms and short terms which became very apparent in late 1957, and certainly it was obvious to all in the spring of 1958. The Treasury moved in in early June, and the Federal Reserve moved in in late June or July.

Mr. OHLENBUSCH. You mean to clear up the market from what was obviously becoming a panic situation?

Representative COFFIN. Yes.

Mr. OHLENBUSCH. That was in the early part of July, I believe.

Representative COFFIN. The question is, if the Government had gone in for purchasing long-term bonds, whether that would not have had a very significant effect in helping to reduce that gap between the yields of the short terms and long terms.

Mr. OHLENBUSCH. Of course, the record is quite clear that there was approximately \$650 million invested in support of, I believe, the one issue of Government securities which had come out in June. But I do not think the subsequent decline that has occurred in the market has been any less because of that purchase. To be sure, a panic situation was averted there, and we could have had some very rough times, had that not been cleared up.

But I think the general statement that one might make would be that as to the ultimate course of the bond market, that changed the ultimate course very little.

Representative COFFIN. Were you people called in, or was the committee, whether you people individually were called in or not, prior to the issue of those 2½ bonds.

Mr. OHLENBUSCH. I do not recall, Mr. Coffin.

Mr. KLAMAN. We would have a record of it.

Representative COFFIN. We know now, do we not, that that was an excessive issue, in terms of what people would buy and keep?

Mr. OHLENBUSCH. We do; yes, sir.

Representative COFFIN. Did you people at the time make any judgment for yourselves as to whether this was going to be too large an issue in terms of what the basic economic conditions justified?

Mr. OHLENBUSCH. Mr. Coffin, as I just said, I do not recall whether we were in on the consultation phases of that issue or not. Had we been, though, the issue which the Treasury offered to the market certainly would have been my recommendation also.

Representative COFFIN. You did not feel that there was a certain amount of speculation in here?

Mr. OHLENBUSCH. Mr. Coffin, I did feel that there was a certain amount of speculation. No one had the slightest idea of how large it had become, and, of course, it became largest in the latter phases, particularly during the first 2 weeks in June. But to answer your question, the issue of 2½ percent bonds would have been my recommendation. It was my recommendation to the bank that we participate in this issue, and we did to a very large extent.

Representative COFFIN. I realize, too, that in this field of hindsight it is always very easy to be much wiser.

Mr. OHLENBUSCH. That is right.

Representative PATMAN. Mr. Widnall, would you like to ask questions?

Representative WIDNALL. Just one question, Mr. Chairman.

Mr. Ohlenbusch, if in the last 12 months the Federal Reserve had maintained the same distribution of age classes in its securities, do you believe the long-term rates would or would not have risen much more in step with the short-term rates than they in fact did?

If they had maintained the same distribution of age classes in securities, do you believe the long-term rates would or would not have risen much more in step than the short-term rates than they in fact did?

Mr. OHLENBUSCH. If Federal had maintained the same age distribution?

Representative WIDNALL. That is right; the 1 year, the 1 to 5 years, the 5 to 10 years, and over 10-year securities.

Mr. OHLENBUSCH. Except for the day or two in the early part of July 1958, I don't know that the Federal made any changes in its port-

folio. It added to and on occasion sold some bills. I don't believe any other changes were made. None that I know of.

Representative WIDNALL. Did they refund the long terms?

Mr. OHLENBUSCH. Wait a moment. A change was made just here within the last few days, on this most recent refunding of Treasury securities, where the Federal held—I have forgotten the amount now—something of the magnitude of \$5 to \$8 billion of the maturing certificates, and the Federal Reserve in the exchange took some of the longer Treasury notes being offered.

This, I think, was a little change in Federal Reserve action. I certainly did not attach any significance to it, other than that I think many of us had felt it an undesirable situation that the Fed holds, as it did, such a large holding of one issue.

I would not attach any significance to this change. I do not think I have grasped your question, though.

Representative WIDNALL. I notice in the report of the Federal Reserve Bulletin, under marketable securities by maturity class, that June 30, 1958, they held in the 1- to 5-year class \$41,071 million, and on March 31, 1959, \$60 billion, for 1 to 5 years. That is a very marked change.

Representative PATMAN. Congressman, are you not mistaken about billions and millions there?

Representative WIDNALL. Millions.

Mr. OHLENBUSCH. The amount in the 1- to 5-year category went from \$40 million to \$60 million?

Representative WIDNALL. Yes.

At the same time, in the 5- to 10-year class, it went down from \$22,961,000 to \$14,797,000.

Mr. OHLENBUSCH. I don't know what would have occasioned such a change.

Representative WIDNALL. That is what I was trying to get in my original question. If they maintained the same age class in securities, whether or not the other would have occurred.

Mr. OHLENBUSCH. I don't think it would have made any difference ultimately.

Representative WIDNALL. That is all.

Representative PATMAN. I would like to ask you how you find out what advice the American Bankers Association and Investment Bankers Association has given to the Treasury before you make your recommendations on these issues.

Mr. OHLENBUSCH. We don't find out, Mr. Chairman.

Representative PATMAN. You don't find out?

Mr. OHLENBUSCH. No, sir. We do not even try to find out.

Representative PATMAN. I am just asking for information. I didn't know. I thought maybe there was a way of knowing. I thought possibly the Treasury made it available.

Mr. OHLENBUSCH. Mr. Chairman, my president sits on the ABA committee and I sit on the Savings Bank Committee. After we have started talking to the Treasury, we do not talk to each other on this problem.

Representative PATMAN. You do not have any unconversational understandings, then.

Would it be satisfactory if I ask you some questions in writing, if I desire to do so, and then you answer them when you correct your testimony?

Mr. OHLENBUSCH. For submission at a later date?

Representative PATMAN. Yes.

Mr. OHLENBUSCH. Very certainly, Mr. Chairman.

Representative PATMAN. Are there any other questions?

Representative WIDNALL. That is all I have.

Mr. Chairman, that figure was billions, not millions.

Representative PATMAN. It was? You were dealing with all the commercial banks.

Representative WIDNALL. \$67,782 million.

Representative PATMAN. Who holds those bonds?

Representative WIDNALL. These are the ownership of U.S. Government marketable and convertible securities.

Mr. OHLENBUSCH. By the Federal Reserve bank?

Representative WIDNALL. By the total, all classes.

Representative PATMAN. You mean the commercial banks, too?

Representative WIDNALL. Yes.

Representative PATMAN. That had to be; yes.

Mr. OHLENBUSCH. I must have misunderstood the question.

Representative WIDNALL. The original question dealt with the Federal Reserve and their holdings and the distribution of their holdings.

Representative PATMAN. There is where I felt it was obviously incorrect.

Mr. KLAMAN. The figure you read includes commercial bank holdings, doesn't it?

Representative WIDNALL. Yes.

Mr. KLAMAN. That is quite a difference. That reflects commercial bank policy and the shifting of the Treasury's offerings from long to short on the refundings.

Representative COFFIN. I have one final question, following up on your colloquy on housing.

Do you think that in the periods of tight money and in rising interest rates or high interest rates, the impact of this on residential construction, would you favor policies to lessen the burden on homeowners—this is not the remedy suggested by Mr. Klamam because that in the short run at least it might increase the burden on homeowners—specifically would you favor liberalized lending by either the Home Loan Bank or FNMA in periods of tight money?

Mr. OHLENBUSCH. Well, I think that if we were to do this, we would have the same kind of undesirable price fixing that we would have when the Government steps in to fix any prices, that they would accumulate a great many mortgages, and probably if this thing were to go far enough would find themselves the only market for mortgages under the conditions similar to those prevailing in 1957.

Representative COFFIN. Would you say that there would be no condition under which the Government should step in through its institutions and relieve the burden on homeowners?

Suppose this made a great impact on the economy that was adverse.

Mr. KLAMAN. What do you mean by relieving the burden on homeowners?

Representative COFFIN. The interest burden.

Mr. KLAMAN. Not on homeowners, but prospective purchasers, do you mean?

Representative COFFIN. Yes, or maybe homeowners with repairs and additions.

Mr. KLAMAN. When you ask that question, Mr. Congressman, don't you have to really ask yourself, "Under what conditions and what markets do you feel the Federal Government should step in to offer some kind of shelter? Why, particularly, will you single out the mortgage market? Why isn't it feasible for the Federal Government to step in and ease the financing of school facilities, which are so essential, of highways? Municipal governments are in a difficult situation when interests rates rise and they can't sell bonds. Why then, do you just single out one market and where do you draw the line on public policy?"

Representative COFFIN. You talk as if we had a completely free market with no governmental influence at the present time. It is not my understanding that we have a completely free market, if anything.

Mr. KLAMAN. Well, there is a difference between completely free and partially free. But once you go in to establish a policy of fixing interest rates, in one area of the capital market only, you are bound to introduce dislocations and fluctuations that we are going to have to deal with for some time to come.

Questions will legitimately be raised why shelter one sector of the economy and not others which are equally worthwhile.

Representative COFFIN. This is obviously too vast a problem for us to get into, because very early, I guess in the first series of hearings, Professor Schlichtor made the point that he would like to see a survey of all the subsidies that exist in this economy today. I suspect the list would be a very long one.

Mr. KLAMAN. One thing I am very conscious of in this sense. As you know, the Government is more involved in housing, perhaps, than in any other sector, outside of agriculture. I think when you compartmentalize, and there is one group dealing with one area, seeking to achieve a particular purpose in one area, and not looking at the other area, we need some group that coordinates overall monetary fiscal policy with all Federal lending agency policy, so that one is not operating at counterpurposes with another.

If you have a situation where it is deemed advisable by whoever is setting the policy to contend with inflationary forces, and another arm of the Government decides to come in and frustrate this through direct lending, either through FNMA or some other system, then you have some frustration of your policy.

Whether the policy is wise or not is not the judgment at hand. The question is how can you operate with one purpose in mind? I think the fixed interest rates really confounds the policy in this area.

Representative COFFIN. I am not going to pursue it, not because you haven't opened up a very good field, but because the two of us have.

That is all, Mr. Chairman.

(Mr. Ohlenbusch subsequently submitted the following for the record:)

THE BOWERY SAVINGS BANK,
New York, N.Y., August 7, 1959.

Hon. PAUL H. DOUGLAS,
Joint Economic Committee,
New Senate Office Building,
Washington, D.C.

MY DEAR SENATOR DOUGLAS: At my meeting with you in Washington on July 29, you requested that I submit certain information regarding this bank's holdings and activities in U.S. Government securities. This material is furnished herewith.

Exhibit I lists our holdings by par value at the end of each year from 1948 through 1958 and on June 30, 1959. It also lists for these years, and the most recent half year, our purchases and sales and redemptions of U.S. Government securities by par values.

Exhibit II, for the last 2 years, shows our purchases and sales of U.S. Government securities and the dealers with whom this business has been done. This tabulation also includes redemptions of Government securities which, of course, are presented to the Federal Reserve Bank of New York as agent for U.S. Treasury. We have broken down this activity into maturity classes showing, separately, figures for transactions involving obligations with less than 3 months to maturity from date of purchase or sale and those with more than 3 months to maturity. The reason, of course, for separating this material in this manner is that obligations with less than 3 months would show a higher turnover ratio by reason of their nature.

I sincerely hope that this information is in the form required for your purposes.

Very sincerely yours,

J. OHLENBUSCH.

EXHIBIT I.—*The Bowery Savings Bank holdings and transactions in U.S. Government securities*

[Par values in thousands]

	Holdings	Year	Purchased	Sold and redeemed
Dec. 31, 1948.....	\$250,835	1948	\$122,288	\$239,288
Dec. 31, 1949.....	334,037	1949	154,884	131,151
Dec. 31, 1950.....	298,511	1950	127,681	163,207
Dec. 31, 1951.....	237,348	1951	98,828	159,992
Dec. 31, 1952.....	239,138	1952	84,952	99,555
Dec. 31, 1952.....	238,132	1953	288,816	273,436
Dec. 31, 1953.....	280,681	1954	343,438	323,937
Dec. 31, 1954.....	281,546	1955	309,682	285,927
Dec. 31, 1955.....	206,271	1956	156,352	232,895
Dec. 31, 1956.....	216,162	1957	323,225	312,977
Dec. 31, 1957.....	217,898	1958	480,758	478,814
Dec. 31, 1958.....	212,436	1959	145,630	152,473
June 30, 1959.....				

† To June 30.

EXHIBIT II.—*Transactions of the Bowery Savings Bank in U.S. Government obligations*

[Par value in thousands]

	Period July 1, 1957, to June 30, 1958				Period July 1, 1958, to June 30, 1959			
	Purchases		Sales		Purchases		Sales	
	Col. 1 ¹	Col. 2 ²	Col. 1 ¹	Col. 2 ²	Col. 1 ¹	Col. 2 ²	Col. 1 ¹	Col. 2 ²
C. F. Childs & Co.....	\$44,600	\$4,000	\$6,500	\$40,000	\$12,500	\$5,200	\$4,500	\$4,000
C. J. Devine & Co.....	37,289	21,065	3,000	61,925	28,000	32,475	10,500	49,637
Discount Corp.....	57,159	78,186	12,159	135,598	12,500	133,206	3,000	137,330
First Boston Corp.....	11,450	25,941	2,000	32,941	1,900	22,407	-----	24,550
A. G. Lanston & Co.....	9,000	25,000	5,000	25,000	9,000	12,500	-----	14,500
New York Hanseatic Corp.....	13,000	4,250	7,000	5,250	3,500	1,663	10,500	1,000
W. E. Pollock & Co.....	9,989	8,200	8,800	0,700	3,750	9,154	2,750	8,488
Charles E. Quincey & Co.....	-----	1,000	-----	1,000	3,250	14,000	1,250	15,250
Salomon Bros. & Hutzler.....	900	15,363	2,700	14,856	-----	49,349	-----	46,422
Commercial bank dealers.....	4,000	2,430	3,200	-----	10,500	5,000	18,500	1,000
Other dealers.....	250	-----	-----	250	-----	1,061	-----	3,070
Total dealer transactions.....	187,637	185,435	50,359	323,520	84,900	286,015	51,000	305,247
Federal Reserve Bank of New York, agent for U.S. Treasury.....	-----	122,109	3 62,739	3 50,109	-----	16,899	3 34,500	3 5,000
Total transactions.....	187,637	307,544	113,098	373,629	84,900	302,914	85,500	310,247

¹ Obligations with less than 3 months to maturity from date of purchase or sale.² Obligations with more than 3 months to maturity from date of purchase or sale.³ Redemptions or exchanges.

Representative PATMAN. Thank you, gentlemen, very much. We appreciate your testimony. We will certainly consider it.

The committee will stand in recess until tomorrow morning at 10 o'clock in this room, at which time we will have before us as a witness the Honorable William McChesney Martin, Jr., the Chairman of the Federal Reserve Board.

(Whereupon, at 12 noon, the committee recessed, to reconvene at 10 a.m., Thursday, July 30, 1959.)

EMPLOYMENT, GROWTH, AND PRICE LEVELS

THURSDAY, JULY 30, 1959

CONGRESS OF THE UNITED STATES,
JOINT ECONOMIC COMMITTEE,
Washington, D.C.

The committee met at 10 a. m., pursuant to recess, in room P-63, the Capitol, Senator Paul H. Douglas (chairman) presiding.

Present: Senators Douglas and Javits; Representatives Patman, Reuss, Coffin and Curtis of Missouri.

The CHAIRMAN. The committee will be in order.

FURTHER STATEMENT OF WILLIAM McCHESNEY MARTIN, JR., CHAIRMAN, BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM; ACCOMPANIED BY GUY E. NOYES, ADVISER, DIVISION OF RESEARCH, FEDERAL RESERVE BOARD; WINFIELD W. RIEFLER, ASSISTANT TO THE CHAIRMAN, FEDERAL RESERVE BOARD; AND PETER M. KEIR, CHIEF OF GOVERNMENT FINANCE SECTION, FEDERAL RESERVE BOARD

Mr. MARTIN. I received yesterday your staff's briefing memorandum from Mr. Knowles, the committee's special economic counsel. I read it last night. I want to say it is a first-class job and presents the issues very fairly and intelligently. I really found it very helpful and constructive. I would just like to put that on the record. (See p. 1245.)

The CHAIRMAN. We are very proud of our staff.

May I make another statement for the record which does not deal with the subject matter this morning.

When we had the representatives of the life insurance industry here, I complained to them of their practice of spreading scare talk about inflation when as a matter of fact the price level during the last year, both wholesale and retail, had been approximately steady.

On the same day that I was examining them, there appeared in the Washington Post a full page ad, depicting a revolver and eight cartridges, with the cartridge clip having this statement on it: "The biggest robbery this country has ever known." This took up two-thirds of the page. Underneath was the statement, "The thief who stole money from 160 million people, stole food money, savings, and keeps on stealing," the question, "Who is the thief? His name is not important. Call him inflation, high cost of living, shrinking dollar or anything you like." Ads like this certainly do not increase confidence in the bond issues of the Government.

In the evening paper, the Star, the same advertisement appeared on page B-20. The Post ad was on page A-24. The Post on July 28, the Star, the evening of the 27th. Needless to say it was issued by the advertising firm of Young & Rubicam. Mr. Rubicam is a personal friend of mine, but I think he is more or less retired from the firm. In the Star for Monday, July 27, there was an ad which took up about two-thirds of the page signed by the Institute of Life Insurance, on "Inflation."

These are just some of the things that have been going on in the nationwide campaign started by the President shortly after the election last fall which went against the Republican Party. It was taken up by the Republican National Committee, followed by many of the Republican newspapers of the country, joined in by life insurance companies, and evidently the campaign is being renewed at this time.

I think it is important that it be understood that the 84th and 85th Congresses cut the President's budget requests by \$8 billion. In almost every case so-called back door financing has been recommended by the administration itself. The latest chapter was the \$4.5 billion authorized for the International Monetary Fund and the World Bank. I believe a similar authorization is being provided for the Inter-American Bank. The deficit of \$12.5 billion for fiscal 1959 was not caused by wild spending Democrats but was the result first, of a \$6 to \$7 billion decline in receipts due to the recession. That was in the field of corporate profits. Second, an increase of \$2.2 billion in the cost of agricultural surpluses and running the Department of Agriculture. Much of this in my opinion was due to the refusal of the Secretary of Agriculture to place any kind of production controls on about 12 crops, especially corn and feed crops. Third, a \$2 billion increase in Defense and Atomic Energy, and fourth, an increase in the unemployment payments which was the direct result of the recession. Despite that, the price level has been as stable as in any period in our recent history.

Now, Mr. Martin, I know you are not formally a member of the administration, but what is happening is that the administration shouts inflation about funds for any social program which they historically have opposed, but they have at the same time billions in the budget in the form of subsidies or tax privileges about which no action is taken. Consequently they imply slum clearance is inflationary.

I want to congratulate you, Mr. Martin, on the honesty of your testimony yesterday before the Housing Subcommittee in which you pointed out that inflationary features in the housing bill were not in the public sector of the bill, but in the private sector of the bill, and in the reduction of downpayments and the extension of the amortization period. But the administration and its defenders are saying that slum clearance is inflationary, and that shipbuilding subsidies are not. Increases in appropriations for research in the field of heart disease and cancer are called budget busting, but the \$500 million subsidy in the form of second and third class mail rates to newspapers, magazines, and direct mail advertisers is not. No doubt an adequate bill for school construction would be vetoed as inflationary, but nothing is said by the administration about silver subsidies, wool subsidies, increased lending capacity to banks by reason of lower reserve requirements, navigational aids to shipping, quotas against oil imports, the oil

depletion allowance, dividend credit, excessive expense allowances, abuses of capital gains, spinoffs, splitoffs, etc., all of which affect the budget either through increased expenditures or decreased revenues because of special tax privileges. The fact is that our opponents have found that they no longer can scare people with the cry of socialism, and have instead substituted the cry of inflation against those social programs which they oppose.

I wish I had some members of the minority here. I think the basic purpose of this publicity campaign and false charges against the Democratic Party is an attempt to kidnap the liberal political victory of 1958 and prevent the enactment of programs designed to help the weak and the poor and reduce the privileges of the strong and well-to-do. I wanted to say that and get it in the record.

I have been somewhat pained by your statement that inflation was imminent and existing. I take it you suffered pain on this point by your conversation in the meeting of the World Bank and International Fund at New Delhi because shortly after that you stated how the central bank authorities of these other countries were distressed at the size of the Government deficit and the prospects of inflation.

Mr. MARTIN. That is correct. I made a speech in December 1958.

The CHAIRMAN. I suppose that people who expressed their concern in this matter were in general virtually the heads of the various national banks?

Mr. MARTIN. And their associates at this meeting.

The CHAIRMAN. It was not confined to Great Britain or West Germany.

Mr. MARTIN. No.

The CHAIRMAN. I would like to make this point. All of these countries have been receiving substantial amounts of foreign aid from this Government. We have borne a heavy burden to help them to be fiscally solvent. This has been a cause of governmental deficit in the last year and the deficits in the preceding years.

Did you find any move on the part of these central bankers of the countries receiving assistance from the United States, who are so distressed at our financial position, to ease that financial position by requesting less foreign aid from us?

Mr. MARTIN. I did not even discuss it with them.

The CHAIRMAN. You did not?

Mr. MARTIN. No, Senator.

The CHAIRMAN. If they were really distressed and felt our fiscal solvency was really in danger, they could have helped us very materially by saying we won't ask for as much money this year, and therefore we will help you to attain fiscal solvency. But there was no such move by them. We strain to the utmost to help them. Nevertheless, we are thought by them not to be fiscally solvent, and this so affected the mind of the eminent chairman of the Federal Reserve Board that he speaks of the loss of confidence which other nations have in us.

You have carried to us their message. I wonder if you would be willing to carry a message back to them, namely, that we are going to make a very large cut in the budget for foreign aid this year. It has been cut by the House yesterday from something over \$3.9 billion to \$3.1 billion. There will be a saving of \$800 million.

I notice the President has made an appeal that the Senate restore a large portion of the cut. I think this is highly problematical. So perhaps you can reassure these gentlemen and make them feel better about the fiscal solvency of the United States by telling them that next year they will get less money from the United States, and therefore there will be less occasion for them to worry about the financial position of the United States. Will you carry that message back to them—a modern message to Garcia, so to speak.

Mr. MARTIN. Senator, most of these representatives in the banks—I might say there will be a meeting of the International Bank and Monetary Fund here in Washington, and I am sure you will be invited to some of those affairs. You might carry the message to them directly.

The CHAIRMAN. If you will point out to me who these gentlemen were who complained about our fiscal solvency, I will be very glad to reassure them, and also tell them that their advice has been carried out. They are improving our fiscal solvency by diminishing the strain which these other countries have imposed upon us.

Representative REUSS. I certainly want to associate myself with this analysis. The Chairman refers to fiscal solvency; that is our own internal budgetary problem. He might add our international balance payments position which is suffering seriously, and in another context apparently causes these international figures to be concerned.

Representative PATMAN. If the Senator will yield for an observation, on the domestic front considering inflation, on yesterday I understand that the House Ways and Means Committee passed out a bill which I think is very bad to, in effect, do away with the pay-as-you-go principle for highway construction. I thought that was one of the most wonderful programs we have ever had, that is, the pay-as-you-go. Now we would provide a billion dollars in bonds to be floated now in competition with all other securities that will be offered.

It occurs to me that, too, will be inflationary right here in the home front. Our committee could very well afford to associate themselves with the position that we should continue that pay-as-you-go program. If we are not going to do it while times are good, when are we going to do it? If we are not going to balance the budget when times are good, and pay something on the national debt when times are good, when are we going to do it? It looks to me that we are beating a retreat on this pay-as-you-go program. I deplore it very much. I look upon it as a deliberate attempt to further unbalance the budget and put our fiscal affairs in a worse condition.

The CHAIRMAN. Has that been carried by the Ways and Means?

Representative PATMAN. That is my understanding.

Representative REUSS. Yes.

Representative PATMAN. I think we should pay as we go just as the law contemplated. Certainly with times as good as they are now, if we are not going to do it, it shows we have no real intent to carry it out. Don't you think that would be highly inflationary, Mr. Martin, this billion dollars for road construction?

Mr. MARTIN. I do, from what you say.

Representative PATMAN. That will be in there with expenditures for Inter-American Bank and other sacred cows.

Mr. MARTIN. You are right down my line, Mr. Patman. I think under present conditions we ought not to only have the budget balanced, but we ought to have a budget surplus.

Representative PATMAN. We ought to have a surplus and pay something more on the national debt.

Mr. MARTIN. I could not agree with you more.

Representative PATMAN. I think the Congress ought to stay in session until the budget is balanced, and properly balanced, and a sum set aside for a surplus to pay on the national debt.

The CHAIRMAN. I agree on that in a period of good times. Now, coming back to the subject matter which we were going into when Congressman Curtis pointed out there was no quorum—and I regret we had to call you back, Mr. Martin, because I hoped we could conclude the day before yesterday—the issue which we were discussing concerned the relative merits of expanding a given increase in the total amount of bank credit by (a) open-market operations and purchase of Government securities, and (b) the lowering of reserve ratios. The point which I was making was, assume that you want to increase the total supply of bank credit by roughly 3 percent a year for a longtime rate of increase, that this is a given amount which would amount roughly, I suppose, to around \$3 billion of bank credit per year. There are two ways of doing this. One would be by lowering reserve ratios so that with the same absolute amount of member bank reserves in the Fed, the banks could then loan and create an additional \$3 billion bank credit, in which event they would collect the interest on this \$3 billion. The Federal Government would get nothing.

The other method would be for the Federal Reserve System to go into the market and buy Government securities. We won't go into the question of whether these are bills or bonds. This would increase member bank reserves, wouldn't it?

Mr. MARTIN. That is right.

The CHAIRMAN. As member bank reserves rose, the lending capacity of the banks would rise.

Mr. MARTIN. That is right.

The CHAIRMAN. Generally, except in severe depression, as you increase the lending capacity of the banks, the banks will actually increase their loans because they don't want idle reserves. That is true, is it not?

Mr. MARTIN. That is right.

The CHAIRMAN. So that the ultimate result so far as the expansion of bank credit is concerned is the same regardless of the method taken.

You said both will have the same end result.

Mr. MARTIN. That is right.

The CHAIRMAN. One difference, at least, is that in the case of lowering the reserves, the banks collect the entire amount of the interest on the added loans thus made, whereas in the second case, it would be necessary to expand member bank reserves in order to get an increase of \$3 billion in bank credit by only approximately \$500 million; is that not right?

Mr. MARTIN. That is right.

The CHAIRMAN. Therefore, the Federal Reserve will have securities worth approximately \$500 million in its portfolio, which it did not have before, upon which it will collect interest. That is true, is it not?

Mr. MARTIN. That is correct.

The CHAIRMAN. It is the practice of the Federal Reserve to turn over 90 percent of its net profits to the Federal Government. So that the increased earnings of the Fed would—nine-tenths of the increased earnings of the Fed—would be turned over to the Federal Government. The income of the Federal Government would thus be increased, and if the budget were otherwise balanced, it could use this added revenue to purchase bonds in the open market or from the banks, and thus reduce the amount of public indebtedness, raising the price of bonds, lowering the yield on bonds—on outstanding issues—hence stabilizing and improving the market for Government bonds.

Perhaps I have not phrased the question the way Congressman Reuss or Congressman Patman would phrase it, but I phrase it in my own fashion. This is what some of us feel very acutely. We are somewhat distressed—perhaps I should say puzzled—by your general implication that to use open-market methods is inflationary, whereas lowering reserve ratios is not.

Then I am puzzled by the statement which you made that you are not concerned—I have to check this on the record—or you did not regard it as one of your functions to make money for the Government. I wonder if you would be willing to state for the record why it is that you would prefer to get the longtime expansion of bank credit by the medium of lowering reserve ratios rather than by open-market operations?

Mr. MARTIN. Senator, let me approach it first by saying that I don't think it should ever be the central purpose of a central bank to make money. It should be to regulate the flow of money in the economy.

The CHAIRMAN. If I may interrupt there, I think I would be willing to accept that. But if you can regulate the flow approximately as well by one method as by the other, and in the process produce revenue for the Government and increase the capital assets of the Government by \$500 million a year, and make an interest gain in addition, why not take on the method which has this added advantage? That is the point.

Mr. MARTIN. I would not quarrel with you on that, if you can. I would only make the statement of judgment as to whether that is possible.

The CHAIRMAN. Why not?

Mr. MARTIN. That is the problem that we are facing. Plus the fact that I think what we want to do is to get lending for business translated into the economy in the way that benefits the economy most effectively.

The CHAIRMAN. Why can't you do it by one method just as well as the other?

Mr. MARTIN. Not quite.

The CHAIRMAN. That is my question. Why can't you?

Mr. MARTIN. In a recession, for one thing, you buy open market securities and the money market banks is where the first impact occurs. In a recession you want to move the reserves into all corners of the country as rapidly as you can.

The CHAIRMAN. We are not speaking of the same thing. You are going into the cyclical policy. I am speaking of secular policy; that is, in the longrun upward movement of bank credit which I think you correctly said is about 3 percent a year. Why can't we effect that by open market operations just as well as by lowering reserve ratios and in addition get revenue for the Government? I am not going into this question of cyclical control, but the longrun policy.

Mr. MARTIN. Alright, let us leave cyclical out and call it secular. The point I am trying to establish is that the 3 percent rate mentioned here is not a mathematical rate. This has been asserted in some literature and discussions as though it were something that were fixed. We have to have some guideposts, and I am not quarreling with the use of that figure. I am saying this—

The CHAIRMAN. These are just rough figures. It might be 2 percent one year, 3.5 another, and so forth. I am simply taking a longrun average.

Mr. MARTIN. I frequently yearn in my position for some automatic formula that would make our job simpler—where we would not have to try to deal with that difficult thing to measure—as you rightly point out—the velocity of money. Also, the concomitant factors that go with it. We have had to try to measure that. It just so happens that in the periods preceding, roughly, the last 10 years, for example, we had been using reserve requirements and had not been using the general controls. That was the history of things up to the time of the 1951 accord. We had high reserve requirements and low pegged interest rates—low in terms of the expansion of the economy. As we moved out of that period and adjustment began, we saw from the previous experience what the result was of using reserve requirements, as such—to increase them and thereby have the additional pressure put on the capital market at the time that the bonds were pegged at par at 22 and 32's in the long-term issues.

The CHAIRMAN. That is a long time back. That is over 8 years now.

Mr. MARTIN. That is where you and I have a little difference of emphasis. I look on this inflation thing as a process that cannot be isolated in parts. I think we have been in an inflationary period in this country virtually since the end of the war. We have had periods where the inflationary pressures have been less, and periods where they have been greater. But trying to unravel the knots in a money market as complicated as ours has been a very difficult task. However, let us not go back to 1951. Let us just take the recent period. In 1958 we were expanding the money supply at 8 percent, and at one point 12 percent, if time deposits are taken into account. Now we have slowed growth in the money supply down as the use of funds has increased. We are under about a 3 percent rate in growth in the money supply at the moment. The velocity factors have shifted. To me that is sounder management.

When we were using high reserve requirements and interest rates were pegged, the banks that needed to get additional capital—

The CHAIRMAN. Please don't talk about pegging interest rates. That is over with. As far as I am concerned, I hope it is permanently over with.

Mr. MARTIN. I know you do, Senator. I am trying to put this in focus. I am saying during that period the banks had great difficulty raising adequate capital and aiding the financial structure of the country with the earnings that they then had. I am not, however, trying to produce earnings for the banks. I am trying to put this in perspective.

If you want to take earnings away from the banks, you can use direct taxes. You don't have to do it by the open market operations of the system. This committee staff memorandum is extremely good in putting the pros and cons of this.

The CHAIRMAN. We certainly do not believe in discriminatory taxation on the banks. I am sure you would not advocate that, and I would certainly not advocate that.

Mr. MARTIN. I am not talking about discrimination.

The CHAIRMAN. You are thoroughly acquainted with this provision of the Constitution that Congress shall coin money and regulate the value thereof. When the Founding Fathers framed this, the only type of money was metallic money. They undoubtedly intended to give to Congress the power to create monetary purchasing power. Then banknotes came in. We had to struggle in the Jacksonian period as to whether private banks would create banknotes and hence create purchasing power. The nature of that is frequently misunderstood by the writers of the financial history of the United States. Essentially what Jackson was seeking was to establish the exclusive right of the Government to create monetary purchasing power. Then came the Civil War. As a means of financing the war, Secretary Chase had to stimulate the purchase of bonds. Secretary Chase gave additional power to national banks to print banknotes equal to their holdings in Government bonds or Government securities. Then the credit system was expanded. Instead of metallic coin, banknotes or printed money and checking accounts came in, and the check became accepted as a means of exchange virtually the same as money. So that now I think in your own reports what used to be called money is now called by you currency, and then you have commercial credit and checking accounts.

Now, is it not a fact that what has happened is that the banks create credit upon the basis of the reserves which are credited to them in the Federal Reserve System.

Mr. MARTIN. That is correct. It has been my contention for some time, and that is where this whole discussion focuses, that the reserve requirements, so far as monetary policy is concerned, of banks generally have been higher than necessary, and particularly with respect to the long-term growth of the country.

The CHAIRMAN. It boils down to this. If the average reserve requirement is 15.5 percent, which I believe is the present, then member banks can create approximately \$6.40 of bank credit, is that not true?

Mr. MARTIN. That is right.

The CHAIRMAN. This means the power of creating monetary purchasing power which the Constitution gave to the Congress is dele-

gated by us through you to the commercial banks of the country, and in return we only ask that 15.5 percent of every dollar accrue to the Federal Treasury. That the other 84.5 cents out of each dollar can go to the banks.

Lest there be any misunderstanding, let me say that I am not an advocate of the 100-percent reserve system, although some 30 years ago, along with Irving Fisher and others, I had a part in developing the theoretical possibilities of a 100-percent reserve system. I am not an advocate of it. When I say I am not an advocate of it, when I say that with my lips, I mean that in my heart, because I don't believe in saying something which hides one's real intent. Let not you be frightened or let not the bankers be frightened that I am going to try to take over this entire problem from you. I do say it is a relatively small commission which the Federal Government is asking, or which we are asking in return for this tremendously valuable privilege which we give to them.

Representative PATMAN. Senator, would you yield on that point?

The CHAIRMAN. Yes. I want to pay tribute to Congressman Patman in this connection, because while we have differed on pegging the interest rate, I want to say Congressman Patman has done more than anyone else in Congress to make it clear that the private banking institutions do create monetary purchasing power.

Representative PATMAN. Thank you, sir.

The commercial banks have about \$18 billion reserves. I have gone into that rather carefully in the last few weeks, and I have discovered that the commercial banks actually paid in only about \$1.5 billion of that. The rest of the accumulation of reserves arose through open market purchases. If that is correct, and I believe it is correct—and I believe the banks got back a large part of that \$1.5 billion—they are not only issuing money and creating purchasing power upon the basis of a 6-to-1 ratio average for all banks of all classifications, or 10 or 12 to 1 by country banks or 20 to 1 on time deposits by all banks, regardless of classification but they are actually creating money upon the basis of \$100 to every \$1 of contributed reserve.

The CHAIRMAN. In other words, they are getting a cut of 15.5 cents on every dollar.

Mr. MARTIN. We are trying to get you another answer to your letter, Mr. Patman. I still have difficulty in getting away from the first table we gave you where we took a \$50,000 bank with \$50,000 capital and surplus, and how they paid it in. How you segregate these reserves I just don't see. We will do our best.

Representative PATMAN. You could interrogate the banks themselves and find out how much they had invested in their reserves. I venture to say that they don't have a billion dollars invested in reserves of their own money. I am willing to give them credit for a billion and a half which they paid in at one time, but they got a large part of that back.

Mr. MARTIN. That is a long and difficult subject.

The CHAIRMAN. Mr. Martin, to come back to this original point, which I think is very important, if the two methods give the same ultimate result which you admit, but one of them in the process yields a gain to the Federal Reserve and to the Government of an average of \$500,000 a year, and added interest earnings which accumulate—as

additional amounts, why not take the method which, giving the same ultimate result, yields large capital gains and large increases in net revenue to the Government.

Mr. MARTIN. Because, Senator we are not dealing with ultimate results. We are not dealing with a mathematical equation that comes out at a certain point. We are dealing with a flow of money of a continuous nature. It just is not, in my judgment, an easy matter, nor is it correct to say that you can regulate that flow just as effectively by something that will come out with an end result in terms of benefit to the Treasury or benefit to the banks.

The CHAIRMAN. First let me say that I think all of us, whether Members of Congress or Government administrators, sometimes err in merely watching the swift flow of events and participating in that flow of events, without concerning ourselves with ultimate consequences. I think we should see the eventual ultimate events so that we at least have some longrun ideas in our heads. If one method or if both methods give the same ultimate results so far as expansion of credit is concerned, but one yields capital gains to the Government probably of around \$500 million a year, on the average, and cumulative interest, why not adopt the open market system? What are its disadvantages?

Mr. MARTIN. The disadvantages are in the current flow of money and credit, which is what we are dealing with from day to day, and week to week. Our judgment may not always be correct. I have never held it out to be. That is what we are attempting to regulate. On the philosophical bent, which you seem to be getting into with respect to ultimate ends, I would like to quote a little Latin: *Forsan et haec meminisse iuvabit*.

The CHAIRMAN. Would you spell that out?

Mr. MARTIN. F-o-r-s-a-n e-t h-a-e-c m-e-m-i-n-i-s-s-e i-u-v-a-b-e.

The CHAIRMAN. What is your colloquial interpretation of that?

Mr. MARTIN. "And perhaps at some later time it will be pleasant to look back on these things."

The CHAIRMAN. The grave is a fine and pleasant place, but there is not much pleasant conversation there.

Senator JAVITS. So far as we know, Mr. Chairman.

Mr. MARTIN. I reiterate, I yearn for some formula that would reduce the problem that we face weekly and daily at times in regulating the money supply to something that we could give as a mathematical equation and say here is where we come out.

The CHAIRMAN. Let me say that you have not yet given me the difficulties of the open market operations. I think I should give you an opportunity if you want to write out a more considered statement.

Mr. MARTIN. I would be very glad to write out such a statement.

(Mr. Martin subsequently submitted the following for the record:)

The overriding aim of Federal Reserve policy actions must at all times be the provision of the volume of bank reserves that is appropriate to the general economic climate of the time. Success in this endeavor has important bearing on actions (1) to avoid either inflation or deflation, (2) to sustain high level employment of human and physical resources, and (3) to foster economic growth. The appropriate volume and availability will vary according to the state of the economy, i.e., as to whether it is sluggish or ebullient.

For the most effective performance of its statutory duties, it is essential that the Federal Reserve System should not be influenced by extraneous considerations having to do with the profits that result from its operations as long as

the public interest benefits. One fundamental factor that denotes the special characteristics of the Federal Reserve banks is that their residual profits ultimately flow to the account of the Treasury.

It follows from this position that member bank reserve requirements should not be used as a means to influence Treasury revenues or to provide a sheltered market for Treasury obligations. They should not be raised or maintained at higher levels than are indicated by sound monetary relationships. The mere suggestion that Federal Reserve actions were governed or affected by such extraneous considerations could impair the reputation of the Federal Reserve System for impartial judgment and affect confidence in the dollar as a medium of exchange.

These fundamental propositions should not be read to imply in any sense whatever that the private banks should not carry their fair proportion of the Nation's expenses. The Congress has the power to tax and if it should ever feel that commercial bank profits from the performance of their operations are excessive it can preempt a larger share of those profits to the Public Treasury through increased taxes on all commercial banks, nonmembers as well as members. This would be preferable to a request or directive to the Federal Reserve System to so operate its policy instruments as to affect member bank earnings, actual or potential, for any reason other than the requirements of a sound monetary policy.

The CHAIRMAN. I think I have been taking up too much time. Congressman Curtis.

Representative CURTIS. Thank you, Mr. Chairman.

I want to say how pleased I am at the tone of this investigation this morning. I think this is the approach that we can use and maybe get some results. On this point that Senator Douglas was making, it strikes me we have two different tools, and the way to answer the question is to figure out what one tool will do and what the other one might do. I do believe there is quite a bit of difference, although they might ultimately accomplish the same thing. One might be a pair of pliers that you might pull something with, and the other might be a hammer. It seems to me that the use of the open market operation is not as reversible or as flexible a tool as the use of reserves. Is that not a fair observation?

Mr. MARTIN. No; I don't think so, Mr. Curtis. I think there is more flexibility in the open market operations than in the reserve requirements generally with respect to reversibility.

Representative CURTIS. Here is the reason I posed that there was not, and I would like to examine that. It seems to me if you are using the purchase of additional bonds by the Reserve System—I should not have said the open market. I should have said the purchase by the Reserve System, or the Reserve System utilizing purchasing of Government bonds as a technique of expanding money—how do you reverse that? Isn't the control out of the Federal Reserve System and really over in the Treasury Department, and indeed into the need for financing a Federal debt? If you created more money through having more bonds in the Reserve System, how would you then cut back on the money supply?

Mr. MARTIN. We would sell, and that is why we have intended to deal in bills or the shorter end of the market, because that is of less upset to the market. A 90-day bill will run off in due course, and it might be that would give us an appropriate time to reduce the money supply.

Representative CURTIS. The economic forces that are at play you have no control over. Suppose at the time you decided you wanted to sell because you wanted to slow down the rate of monetary increase

was the very time the Treasury, for other reasons, had to market more bonds?

Mr. MARTIN. This is one of our difficulties. Perhaps we would have to postpone what we would like to do at that time.

Representative CURTIS. Exactly. It seems to me in your control over the reserves that is completely within your power, while the other you have to work out in accord with another independent group. Is that observation correct?

Mr. MARTIN. Not completely. That is the problem on reserve requirements that we have. It has been pointed out that we have tended to reduce reserve requirements, but not to raise them since the 1951 accord.

Representative CURTIS. That is right.

Mr. MARTIN. Previous to the accord, we had raised reserve requirements a number of times, and it had put such pressure on the bond market indirectly. Let us put it this way. Here is a bank. The reserve requirements are raised at a time when credit is expanding. That does not mean that the bank, to supply those reserves, or when it gets those reserves, is necessarily going to curtail lending to some customer that they may wish to serve. They may decide to sell securities out of their portfolio. Some of those securities at that time, or most of them, were Government securities. So that just collapsed the Government security market on us.

Representative CURTIS. I am going to join the chairman's request, if you would, that you spell it out from a different approach. As I understand, the chairman says you can accomplish the same result by either of the two.

The CHAIRMAN. If the Congressman will permit me, Mr. Martin has said that the end result is the same.

Representative CURTIS. I am not disputing that. As I say, that has been pointed out. My question now is that two tools can produce the same results, but the use and the character of the tool, one can be clumsy for a certain thing and the other can be very suited for it. I am really curious because I don't know anything about this subject—I have not been in this monetary field at all—as to the flexibility of the two tools. The point I was trying to raise was this: It seemed to me that in the one you were pretty much your own boss, under the power that Congress gave you, that is, the Federal Reserve. In the other, it was one that you had to constantly work closely with an entirely independent agency, the Treasury Department. I see that there could be an area of distinction between the two kinds of tools there. There must be other differences that I don't know.

Mr. MARTIN. We will be glad to prepare a paper on that. I want to make one point clear, however. In our judgment both of these tools are necessary.

(Mr. Martin subsequently submitted the following for the record:)

Theoretically the Federal Reserve System can supply reserves to, or withdraw reserves from, the money market on its own initiative either by purchasing or selling U.S. Government securities or by lowering or raising the reserve requirements of member banks. Technically the use of either instrument of policy can be adopted to achieve a desired level of net free or net borrowed reserves. It follows that after the operation has been concluded the mathematical expansionary effect and the mathematical restrictive effect on the money supply of the net free or net borrowed reserve position, so achieved, would be the same. Here the technical similarity ends.

In a number of respects, use of changes in reserve requirements to effectuate monetary policy differs from resort to open market operations, as follows:

A. METHOD OF DIFFUSION

A major difference is that a change in reserve requirements affects every member bank directly and immediately with equal force, irrespective of differing individual situations or conditions whereas the effects of an open market operation are felt individually and gradually by the member banks through the operation of market forces. For example, sales of securities in the open market may be reflected in withdrawals of deposits at some banks by some customers. The banks' adjustment to these withdrawals may involve sales of securities, which lead to deposit withdrawals and reserve losses at still other banks. In general, the most extended banks will feel the additional pressure most, but it is not possible to trace meticulously the direct chain of impact of an open market operation.

B. SIZE OF OPERATION

Open market operations lend themselves much more readily than do changes in reserve requirements to achieving small changes in the availability of reserves. They can be used readily to provide or withdraw reserves on any given day in amounts that vary from as much as \$100 million (and frequently very much larger amounts) down to figures as small as the denominations of the securities that are traded. Changes in reserve requirements, on the other hand, because they are made as percentages of very large sums, normally change the availability of reserves by very much larger amounts. In the future under the new legislation, any change in the percentage will apply, at the very least, to one of the following four categories of deposits (using most recent figures as illustrations):

[In millions]

	Net demand deposits	Time deposits
Reserve city (including central Reserve city) banks.....	\$66, 134	\$28, 481
Country banks.....	36, 892	25, 488
Total.....	103, 026	53, 969

As a general rule, changes in reserve requirements, to be equable, must be generalized to include all net demand deposits or all time deposits. Even if such a change were as small as one-quarter of 1 percent, which is much smaller than has been used in the past, and it were applied to net demand deposits, it would supply or withdraw bank reserves in the amount of \$257 million in one operation. If special circumstances permitted an adjustment to be made in reserve requirements of either Reserve city member banks or of country member banks alone (and this would not happen frequently), an adjustment as small as one-quarter of 1 percent would involve \$165 million if it were confined to the new class of Reserve city member banks, and \$92 million if it were confined to country member banks.

These illustrations are in terms of changes of one-fourth percentage points in reserve requirements, one-half is the smallest ever applied to date to member banks. One can, of course, by resorting to smaller and smaller fractions in theory make changes in reserve requirements appear capable of as minute adjustments as changes induced by open market operations. Very small fractional changes at relatively frequent intervals, however, would create very difficult problems of adjustment for member banks and would almost certainly be disruptive to the smooth flow of credit in the market.

This factor of size of impact is one reason why it is more difficult to use an increase in reserve requirements to contain a boom than it is to use a decrease to combat a recession. If an increase in reserve requirements is imposed at a time when member banks' holdings of excess reserves are low, or completely offset by borrowing at the discount window, there are only three options open to the banking system to achieve compliance: (1) by wholesale liquidation of loans in an amount several times the increase in reserves required (about six times at present), or (2) by sales of U.S. Government securities in comparable volume

(i.e., about six times at present) to nonbank investors, or (3) by borrowing at the discount window a sum equal to the amount involved in an increase in reserve requirements. In the case of any combination of these, lower prices for U.S. Government securities could be expected. From the moment of the announcement, there would be a strong tendency for potential buyers of U.S. Government securities to defer their bids, thus tending to provoke a disorderly market that would force intervention by the system open market account. Such intervention to restore orderly conditions might require purchases in greater amounts than were involved in the original increase in reserve requirements. As a result, the effort to combat overexpansion in a boom by reducing bank liquidity might induce disorder in the market for Treasury issues and, subsequently, a situation of even greater bank liquidity than had prevailed before the restraining action was initiated. These same problems do not arise when reserve requirements are reduced.

There are occasions when a lowering of reserve requirements may be superior technically to an open market operation. For example, one such occasion arose very suddenly in June 1953 when a series of unforeseen developments in connection with Treasury tax payments produced a situation which needed a very large injection of reserves in a very short period. The reduction in reserve requirements ordered at that time exactly met the technical requirements. It is doubtful whether purchases of securities in the open market would have achieved a similar result.

C. IMPERSONALITY OF OPERATION

It is important that operations undertaken to effectuate the broad purposes of monetary policy be as impersonal as possible in their impact on various segments of the economy. They should affect broadly the availability and cost of borrowing and the return obtainable on saving in general rather than any particular form of borrowing or any particular type of saving.

From the point of view of impersonality, changes in reserve requirements are, in one sense, more impersonal than open market operations which, in addition to changing the availability of reserves, also add to or subtract from the volume of particular types of securities in the market. To the extent, however, that open market operations are confined to short-term securities, these operations are also, in practice, quite impersonal in their effects.

Changes in reserve requirements are not at all impersonal in the extent to which they affect the competitive position of different types of banks. They affect directly only member banks of the Federal Reserve System. Nonmember banks which are subject only to State-imposed reserve requirements are left untouched unless the State requirements are varied automatically with those of member banks.

When resort is made to the open market instrument, the reserves are removed through an impersonal market transaction. The actual absorption of reserves from the market results from the sale of securities to a willing buyer. Thus, the first impact of an open market operation comes about because a transaction has been effected between a willing buyer and a willing seller, rather than as a result of a change in an official regulation. Apart from the publication of Federal Reserve statements, commercial banks are not aware of the absorption of reserves by Federal Reserve. Reserve losses to individual banks take the form of adverse clearing balances, which frequently occur in the normal course of business.

D. EXPECTATIONS

There is one major respect in which member banks seem to react differently during a recession to the provision of a given amount of excess reserves according to whether the stated excess is the result of a series of purchases of U.S. securities in the open market, on the one hand, or of a reduction in reserve requirements, on the other. This is in addition to the fact that a reduction in reserve requirements places additional lending power in all member banks simultaneously.

It seems to be expected generally that an increase in reserve availability brought about by a change in reserve requirements is likely to be more permanent and that the added lending power will not be quickly withdrawn. Member banks, consequently, are likely to react more positively to a reduction in reserve requirements by moving promptly to expand and also to incorporate additional permanently desirable assets in their asset structures. They will be

more likely to expand their long-term assets by purchasing mortgages and also to make customer commitments extending longer into the future, commitments for term loans, for new lines of credit, and for future mortgage financing.

This differential response has both favorable and unfavorable characteristics. It undoubtedly facilitates the quick adoption by businessmen of plans that lead toward expansion and emergence from the recession. It may, at the same time, however, commit the commercial banks to future extensions of credit that they would later rather not have made.

For example, a great many of the bank lines of credit that financed the very rapid expansion of installment credit in 1955 were entered into during the third quarter of 1954 at roughly the same time that reserve requirements were lowered. It will never be possible to prove a cause and effect relationship between these two developments, but experience in both 1954 and again in 1958 suggests that this type of response on the part of member banks does accompany reductions in reserve requirements and that it may be quite dramatic on some occasions.

E. LONG-RUN REDUNDANCIES OR DEFICIENCIES OF RESERVES

In 1927, the long inflow of gold from abroad after 1920 and the low rate of increase in currency in circulation as the use of checking accounts became more general finally reduced the demand for Reserve bank credit to a point where there was a danger that the Federal Reserve banks would lose operating contact with the market.

Should such a contingency recur, it would constitute a clear technical case for increasing reserve requirements, the increase to be effectuated preferably in a period when reserves were redundant. Resort to the reserve requirement arm would be indicated as a technical matter because the Federal open market account would not be in possession of sufficient securities to operate effectively on the side of restraint in the market. The increases in reserve requirements in the thirties represent an adjustment of this type.

A reverse technical situation would occur if growth in world output and correspondingly in world demands for gold as reserves should exceed additions to world gold stocks in such a way as to result in a deficiency of world gold supplies relative to needs for monetary reserves. Under such circumstances, a reduction in reserve requirements against deposits might be in order.

F. RELATION TO TREASURY OPERATIONS

With respect to the System's ability to act independently in pursuit of its statutory responsibilities, there is little difference between its use of open market operations and reserve requirements. The System does, in fact, take into account, in either case, Treasury financing activities, endeavoring to interfere with these as little as possible while pursuing its own objectives.

As pointed out earlier, however, because of their greater flexibility and the fact that their magnitude can be adjusted to current market developments, open market sales are less likely than reserve requirement increases to create market conditions unfavorable to a Treasury operation.

Representative CURTIS. I think you have made that clear.

Mr. MARTIN. I don't want any misunderstanding on that.

Representative CURTIS. I think you have made it clear. Certainly you have made it clear to me. One of the points of dispute I have with Senator Douglas, and certainly with Congressman Reuss, is the feeling I had that they were trying to create the implication that the Federal Reserve was not using at all whatever powers it had to go in the bond market. It is a matter of degree again.

The CHAIRMAN. The Chairman of the Federal Reserve Board has said that he prefers to get a longtime increase in bank credits through lowering reserve requirements and he regards present reserve requirements as too high. I think that is the statement of the Chairman.

Mr. MARTIN. I said under present conditions we have tended to work that way. As I have also indicated, if there were a heavy inflow of gold, for example, there is no question that we would use the

reserve requirements. That is a clear-cut case where that would be used explicitly and promptly.

The CHAIRMAN. You mean raise reserve requirements?

Mr. MARTIN. That is right.

The CHAIRMAN. That raises another point. What about the effect of increasing reserve requirements? That has an incidental effect of increasing the commission which the Federal Treasury gets for the creation of bank credit by the member banks. If you were to raise the requirement to an average of 20 percent, let us say, this would mean that instead of the reserve and hence ultimately the Government getting 15.5 cents of each dollar of bank credit created, it would get 20 cents. So that the division instead of being 84.5 and 15.5 would be 80 and 20. If you value reserve requirements as having a flexible effect when they are reduced, don't they have the same great flexibility when they are increased, or is it like the farm program, it only flexes downward?

Mr. MARTIN. Senator, I followed your statements on this matter, and others. I just cannot understand how anyone can think—I am quite sincere on this—that at the present time if we raised reserve requirements it would do anything but knock the props out from under.

The CHAIRMAN. I am not urging that. I want to make it clear I am not urging that. I am saying that is a theoretical question. I would say if you want to expand bank credit at the present time, the way to do it is to carry out open market operations rather than lowering reserve requirements. That is the position of Congressman Reuss, Congressman Patman, and myself.

Mr. MARTIN. I understood you on other occasions to say that we should have raised reserve requirements.

The CHAIRMAN. Not so much that, I think, as that you should not reduce them.

Mr. MARTIN. I misunderstood that.

Representative CURTIS. I wanted to ask one other question. I am sorry, Mr. Chairman. I was a little late, but I understand that the question was posed to you, Mr. Martin, in regard to this highway program, and you responded that you thought it was inflationary. What I wanted to find out is, What was it you said was inflationary about this highway program?

Mr. MARTIN. Mr. Patman made a very excellent speech on balancing the budget, and getting a surplus and doing everything possible to get our finances in better shape at the present time, and in the course of that he said he saw—but I have not studied the bill—that this highway program had been changed from a pay-as-you-go to a borrowing program.

Representative CURTIS. You said if it had been changed from pay-as-you-go to borrowing, it was inflationary.

Mr. MARTIN. That is right.

Representative CURTIS. I agree with you. The only trouble is that it has not been pay as you go since the Congress acted in 1958. I suspect that Congressman Patman voted for taking it off the pay-as-you-go program in 1958. I happened to be one who voted against it and was accused, as usual, that thereby I was against highways.

The situation that the Ways and Means Committee is confronted with is a question of fiscal integrity. If we do nothing we are going to have \$250 million of contract obligations we can't meet. Not future contracts, but actual contracts that we won't be able to pay for. That is No. 1.

No. 2, the Congress in the 1958 act told the Bureau of Public Roads and the States to accelerate a program by \$1.6 billion with no financing. They told them to increase what was a \$25 billion program by another \$400 million. They likewise put their stamp of approval on a switch in estimates. The trust fund was based on a \$25 billion figure, they accepted a \$36 billion figure, and prorated that figure over the same number of years. That is what we are confronted with. Our choice is increased taxes, short-term revenue bonds, or out of the General Treasury, or do nothing. I think most anyone would agree that we can't do nothing if the fiscal integrity of the United States is at stake. Of the three choices, frankly I don't think any of the three have much to choose from as far as inflation is concerned. Which would be less inflationary in a boom period is moot. The thing that is inflationary is the program itself.

I am happy to say this because I had quite a bit to do with it. As a matter of fact, it has worked out about the way I thought was the best way. The essential thing is that we cut the program back. Instead a new allocation of \$2.5 billion in 1961, it is \$600 million. That is deflationary, I would say, over what was existing. Certainly the cutbacks that we have made in the program along the line of expenditure are nothing but deflationary.

I would like to ask, though, whether we do have a choice as to methods of financing. In some respects, I would have preferred an increase in taxes. Incidentally, I voted for the proposals in Ways and Means to increase taxes, and 6 out of 25 members of the Ways and Means Committee voted that way and 19 against. I voted for every single proposal, although I was not sure that taxes in this boom period were a less inflationary measure than the short-term revenue bonds. They are very definitely limited to the trust fund anticipated revenues. We have the trust fund back, I hope, to a \$25 billion concept. These bonds, as nearly as I can figure, would be limited to about 5 percent.

Representative PATMAN. May I ask a question, Mr. Curtis?

Representative CURTIS. Yes.

Representative PATMAN. What rate of interest will they pay?

Representative CURTIS. We don't have any idea. We have not gotten into that detail. All that happened is that the Ways and Means Committee has taken this action and told the Public Works Committee: "This is what we think we can do from a fiscal standpoint. Are you willing to cut the program back to the cloth that we see we can give you?"

Far from being an inflationary move, I am very proud of the Ways and Means Committee for facing up to the situation. I think the bill in itself is very deflationary.

There is one other comment. One of the theories of the acceleration of the program of \$1.6 billion is that we are going to decelerate at some time. What better time to decelerate, I would say, than in a period of economic boom. I think that is a fair comment, too. If we

ask in 1958 and 1959 for the States to step up their expenditures, and now that we are in a period of boom, it looks to me that is the appropriate time to cut back. If we do nothing because of very poor planning, we go to absolutely no allocations for 9 months. That to me is uneconomic. The damage created of just going from here to now, that is. That is why I was willing to go along with an easing off rather than a complete cutoff, plus taking care of the \$250 million that we are obligated to.

Mr. MARTIN. Let me make clear that I have not even read the bill, as I indicated earlier.

Representative CURTIS. I just wanted to be sure because I suspect that we are going to have the same thing happen every time the debt-ceiling bill comes up. Every time there is an interest ceiling bill up, the people who created the situation seem to be the ones who seek to hide from the results of their actions. Those of us who try to face up to it, which I have done by urging my colleagues to vote the debt limitation to go up, to take interest ceilings off, we are the ones that have to bear the brunt of the attacks from the same people, of saying that we are trying to increase interest rates, or that we want to increase the Federal debt, or, as in this situation, that we want to make things more inflationary. All I ask is that the people who created this fiscal situation stand up and be counted. I have voted against these expenditure programs. As a result I have been accused of being against widows and orphans and sick people and highways and schoolchildren and everything else.

Representative PATMAN. I want the gentleman to yield to me for a question. Does the gentleman contend that the issuance of a billion dollars of additional revenue bonds is not inflationary?

Representative CURTIS. I say in context the thing that creates the situation that calls for either increased taxes, issuing bonds, or going to the Federal Treasury for these funds, that situation is inflationary.

Representative PATMAN. You mean the issuance of the billion dollars' worth of bonds?

Representative CURTIS. No; I didn't say that. I said the situation that creates the necessity for managing this debt either through additional taxes, through short-term revenue bonds or from deficit from the Treasury, that is the situation that is inflationary. How you handle it, whether you use the method of taxes, short-term revenue bonds, or deficit from the Treasury, which is the least inflationary method of the three, is the question that we have to resolve. It is very unfair to insinuate that because we are forced to take one of three or be fiscally irresponsible, that thereby that act is the inflationary act. That is not the act that is inflationary. It is the 1958 act that is the inflationary thing.

I would ask the gentleman which of the three methods does he think is the least inflationary. Frankly, I can't tell. I don't really know whether increase in taxes would have been less inflationary.

Representative PATMAN. An increase in taxes would be less inflationary.

Representative CURTIS. In a period of prosperity?

Representative PATMAN. Yes; surely. It would be less inflationary than issuing bonds. There is no doubt in my mind.

Representative CURTIS. I know that the gentleman can resolve these things in a hurry, but I can't.

Representative PATMAN. I just believe that way.

Representative CURTIS. Would you say from the General Treasury?

Representative PATMAN. I will say that a billion dollar increase in bonds is inflationary, and the gentleman does not deny it. That is what we were talking about.

Representative CURTIS. The gentleman has denied it because it is out of context. That is not the inflationary thing. The inflationary thing is the debt that has been created. How you manage the debt that is created can be done in several ways. I think it is a fair subject for discussion as to whether in this economic period right now the taxes would be or whether these short-term revenue bonds, which ties this into the trust fund concept, or from the General Treasury—which of the three is more inflationary.

Representative PATMAN. Let us just kill one snake at a time. These revenue bonds are inflationary. I advocate pay as you go.

Representative CURTIS. If the gentleman from Texas and his colleagues would quit breeding the snakes, maybe we won't have so many to kill.

The CHAIRMAN. Congressman Patman.

Representative PATMAN. I am glad that we have agreed on this, Mr. Martin. I am glad that we can agree that a billion dollars' extra bonds are inflationary.

Mr. MARTIN. I would prefer taxation.

Representative PATMAN. As to the 1958 act, I want to take a moment to answer Mr. Curtis. As to whether or not a wrong was committed in 1958, the issue then was doing something to get us out of a depressed condition and to encourage the building of highways at a more rapid pace. That was the issue then, to get us out of a depressed situation. If we made a mistake then, let us not make two mistakes. If we made a mistake in 1958, let us correct it in 1959, but let us get back on the pay as you go. It is within our power to do it. Times are good, times are prosperous, earnings of all businesses and corporations are greater than ever before probably in history. If we are not going to balance the budget now, if we are not going to pay as you go now, when will we pay as you go? I am greatly disappointed in the Ways and Means Committee, and the gentleman's own attitude in trying to justify the issuance of a billion dollars' worth of bonds now in competition with all of the billions of dollars that have to be issued by States, counties, political subdivisions, and by the Federal Government, to take care of these commitments. It is bound to be very inflationary. I know the gentleman generally is on the conservative side, and against inflation. But he has now taken the position that inflation is a good thing.

Representative CURTIS. If I have ever heard an unfair presentation of a case, that is it. I do want to say this to the gentleman. I actually did urge that we accelerate the highway program in 1958. That aspect of the bill I had no quarrel with. I voted against it because we were not providing the methods of paying for it sometime in the future when we did get into a boom period. The gentleman says two wrongs don't make a right. The point is that we have done this as an antirecession measure, and now we are confronted with the situation of paying for what we have done. I want to say this again. I was confronted as one who voted for a tax increase in the Ways and Means

Committee, and on the gentleman's side 15 of them, 3 times in row—that is 45 votes—we got 2 votes out of those 45 votes for increased taxes.

Now I am confronted with a situation as one who believes in fiscal integrity of not having had the choice I would have liked, but then what can we get to pay for this obligation that has been created? There is only one other choice, and that was it, unless you want us to do nothing, which is maybe what we will do.

Representative PATMAN. Since the gentleman has boasted about the fine attitude of the minority of the members, I venture to say that none of them introduced the President's proposal of increasing the gas tax.

Representative CURTIS. May I comment just one thing, and then I will cease. No; they did not, and for this reason: Up to that time the President had made no proposal at all of cutting back the program. The quid pro quo that we insisted on for doing something about this temporary situation was a cutback in the program. The actual tax measures that were presented in the Ways and Means Committee had as part of them cutting back on the program. That is why I supported them.

The CHAIRMAN. Would it be acceptable if this colloquy between Congressman Curtis and Congressman Patman be printed at the conclusion of Mr. Martin's testimony so it will not disturb the continuity of the questioning?

Representative PATMAN. Let us put the Senator's over there, too.

The CHAIRMAN. Certainly.

Representative CURTIS. Except in one respect. I did refer to Mr. Martin at the beginning of what he had said.

Representative PATMAN. I don't see any reason why it should not go there. Mr. Martin will not object to it. It does not make a bit of difference. It is just an exception without a reason, the way I see it.

The CHAIRMAN. All right. Mr. Martin, I am very glad to join you in the ranks of the foes of inflation.

Representative PATMAN. I am happy to be in the same position.

Representative REUSS. Before we leave this, I would like to commend my friend, the gentleman from Missouri, Mr. Curtis, who evidently came in and was told that Mr. Patman and Mr. Martin had agreed on something, and was interested to get to the bottom of it.

Representative PATMAN. Mr. Martin, I want to ask you this: We had the hearings on the financial institutions bill in 1957, and I asked you a number of questions there about the attitude and the conduct of these Federal Reserve banks in advertising that they own the Federal Reserve System.

Mr. MARTIN. You are talking about the member banks?

Representative PATMAN. No; I am talking about the 12 Federal Reserve banks. I showed you some of the literature they got out to show that they were claiming to the people that they owned the Federal Reserve System; that the member banks owned the Federal Reserve System.

Mr. MARTIN. Yes.

Representative PATMAN. One of them had a questionnaire that they tested the people on. The answers were to be to this question, the 10th question:

Capital stock in Federal Reserve banks is owned by: (1) Treasury Department, (2) Federal Government, (3) its member banks.

The point they were trying to put over there was that the people are often mistaken. They felt the Treasury Department owned it, the Federal Government owned it, but really the member banks owned the Federal Reserve banks.

I then questioned the propriety of expenditures by a government institution for such purposes. I wonder if you have contacted any of those banks about the kind of literature which they sent out which was misleading to the extent that they said that the Federal Reserve banks were owned by the member banks.

Mr. MARTIN. Your comments on that and that testimony was given to all the presidents of the 12 Federal Reserve banks, and it was discussed with all the presidents.

Representative PATMAN. Thank you, sir. I am glad you did that. The way I see it, and I believe you would see it the same way, these are really public funds. If you spend them for different purposes, even scholarships and things like that, that a postmaster could not spend public funds for, I think it is wrong. I am glad that you called this to the attention of the presidents of the banks and the others, because they are engaged in the expenditure of public funds in ways and for purposes that cannot be condoned.

Mr. MARTIN. Mr. Patman, under the law each of the 12 Reserve banks has its own board of directors and—

Representative PATMAN. That is right.

Mr. MARTIN. We have all this under constant review, and I, in disagreement with you, think we are one of the best audited organizations that I know of.

Representative PATMAN. Add "self-audited," and I will agree. It is as good a self-audited organization as you will find.

Mr. MARTIN. Auditing of the type now going on is really what is essential in the Federal Reserve. We have outside public accountants that are brought in. We have had Arthur Andersen and we have had Price-Waterhouse that have audited. We have made available to you and you have had the audits of the Federal Reserve Board and the Federal Reserve banks. These outside auditors have also gone to the individual Reserve banks to check on our audits and to see whether all the items are covered.

Representative PATMAN. Yes, sir. I have discovered that the audit is lacking in many respects. That is the reason I would like to see the General Accounting Office audit the Federal Reserve System.

Mr. MARTIN. Our auditors do not think so. We do not think so.

Representative PATMAN. I know that is your attitude. I have introduced a bill to that effect, and I am going to press it, because I believe it is in the public interest. I don't think that public money should be handled without the General Accounting Office or some independent audit of it.

Mr. MARTIN. Under our auditing procedures, we are having both a self-audit and an independent audit. I think we are one of the best audited organizations that I know of. As you can testify, there has never been anything in connection with the System that we have withheld from you or any other proper person when we have had inquiry about it. We cannot always dig it up in 24 hours when you go back to 1914. As you know, whatever mistakes we may make are not hidden away. Whatever mistakes of judgment there are, we try

to correct them as rapidly as we can. I don't think we have made an undue share of errors of judgment in our administrative activities. I believe that the banks have been conducted—I am talking about the 12 Federal Reserve banks—extremely efficiently.

Representative PATMAN. Mr. Martin, I think you are clearly wrong. I know you are sincere in believing that you are conducting the affairs properly and that the banks are. I think it has been conducted in such a loose fashion that the presidents of these banks feel that they can spend public money for any purpose for which any private corporation could spend money. In fact, they actually argue that. When I gave out a statement recently showing the loose way in which these public funds were handled, and wasteful and extravagant waste, some of the presidents of the banks were brazen enough to say, Why, sure, they spent money that way, because private concerns spent money that way, and as long as they did what other private concerns were doing, it was all right. They honestly believed it. They failed to put themselves in the position of a postmaster in the town in which they were located but they really are in that public position. They have no more right to spend that money than the postmaster has a right to spend the money that he collects in the sale of stamps. It is all public money. They should not be allowed to believe that they can spend it in an extravagant manner. To that extent, I am disappointed in the Board of Governors for not doing a little brainwashing, educating the regional banks about what the law is on handling public funds.

Mr. MARTIN. I want to make this very clear, and I want it on the record, that I deny extravagance or misuse of funds in any form by the Federal Reserve System.

Representative PATMAN. Naturally you would, Mr. Martin.

Mr. MARTIN. That is all right. If I did not believe it, I would not make that statement.

Representative PATMAN. You saw the many items that I picked out of your own audits, and you do not justify all of them, do you?

Mr. MARTIN. Mr. Patman, those items are being gone over item by item. I would say that many of those items were taken completely out of context, and it was not in my judgment a fair press release.

Representative PATMAN. I know.

Mr. MARTIN. You are raising the issue now, and I am merely putting it to you directly.

Representative PATMAN. They were quoted from your audits volume and page.

Mr. MARTIN. We have all these auditors give us their honest judgment, and we do not withhold anything from you. All I say is that the matters as listed by you were taken, in my judgment, out of context. We will in due course, as we always do, have a response to the House Banking and Currency Committee, to every one of the items that you raised and state what our judgment is. We are in process of working on that now.

Representative PATMAN. I wish you would make it and I wish you would agree to having the General Accounting Office make an audit of the system, because the audits you make are not complete. They are not the kind of audit that a Government auditor would want to make. The General Accounting Office would really give you an audit, and

I hope you agree for the General Accounting Office to audit the Federal Reserve System, and the Federal Reserve Board. If it is as you think clean as a hound's tooth, you have nothing to fear, and I don't see why you should not agree to it. It is public funds. It is a public institution owned by the Government, and there is no reason why you should not do it.

Mr. MARTIN. We have been over this many times, Mr. Patman, as you know. The Banking Acts of 1933 and 1935 covered this particular issue at considerable length. I again say that I think it would be a serious mistake to do that, because I think the central bank needs this authority and it was recognized in the Banking Act of 1933 and carried forward in the 1935 Banking Act. The impression that we are not audited is entirely incorrect. We are very carefully audited. Our expenses are gone through with a fine tooth comb. I don't hold out perfection for the System, and never have. But, I do not think it ought to be done. I believe if it should be done, it should be made a part of the Federal Reserve Act, and put into the Federal Reserve Act as such. At the present time the law does not provide for it.

Representative PATMAN. In 1933 and 1935 our country was suffering from the most serious depression in all history and proposals were made to change the banking laws. Congress hardly looked at it. There was very little discussion of it. It went through with little discussion, because everybody wanted to cooperate to do everything possible to get the country out of the depression. A lot of things as a result got into that 1933 and 1935 act that should not have been tolerated. No general monetary hearing has been conducted in the Congress since that time. If there had been a lot of these things would no doubt have been gone into.

On these audits, I would not say that they are erroneous or deceitful, but they are not full and complete, Mr. Martin. I don't know what the instructions to the auditors were. Did you give them instructions to go into everything that they thought was material and important and should be disclosed? Instructions to private auditors that you have selected, and the freedom and judgment of Government auditors to make an audit is quite different. When you audited the Chicago bank, you used some of the people in the Chicago bank to do the auditing. When you audited the New York bank, you used some of the people in that bank to help do the auditing. I think every audit will disclose that you used some of the people inside the very institution they were auditing in order to help. If that is the right kind of auditing, all right, but I did not think audits ought to be conducted that way. I thought one had outside people to do the auditing that had some sound professional reason to pick out wrongs and irregularities and dishonesty, if any, and thefts, if any, and embezzlements, if any. These auditors don't seem to be charged with that sort a dedicated duty.

Mr. MARTIN. Mr. Patman, you play down one inquiry, of which you were chairman, that was conducted in 1952 for quite a period of time, in which all of these points were raised, and all of them were discussed at considerable length. I don't think there are any legitimate charges of embezzlement or theft or anything of that sort.

Representative PATMAN. No.

Mr. MARTIN. You have been using the words.

Representative PATMAN. I say, if any.

Mr. MARTIN. All right, if any. But there has not been any.

Representative PATMAN. You don't know because you have not audited them. Your own people have been doing the auditing.

Mr. MARTIN. I don't think Price-Waterhouse are our own people. I don't think Arthur Anderson & Company are our own people.

Representative PATMAN. They used some of your own auditors in helping them. Your reports show that.

Mr. MARTIN. They use office boys, too. You use office boys in the Congress.

Representative PATMAN. You are getting off the subject now.

Mr. MARTIN. No.

Representative PATMAN. They used people inside the banks.

Mr. MARTIN. In this matter of auditing you can spend a lifetime in it. I am not a professional auditor, but I have had a lot of experience with it. I have dealt with it in a great many situations, not only with the Federal Reserve, and it is not a simple matter. I insist that the auditing of the Federal Reserve System as done today is a first class job. That is my judgment and I give it to you. If I did not believe it, I would not say so.

Representative PATMAN. I believe you made some statement about the investigation of 1952. Up until then I don't think the Board had ever been audited, had it?

Mr. MARTIN. Yes. You are getting back at the history. At one point we had the General Accounting Office on the Board on part of our accounts. That was discontinued in the Banking Acts of 1933 and 1935. You indicated they did not know what they were doing, but Congress changed the law.

Representative PATMAN. It was not the General Accounting Office on the Board. It was the Comptroller of the Currency on the Board.

Mr. MARTIN. No, not on the Board. The General Accounting Office was not on the Board, but they did audit some of our accounts prior to 1933. The Comptroller of the Currency and also the Secretary of the Treasury were ex officio members of the original board.

Representative PATMAN. I say they were up until 1933.

Mr. MARTIN. But I am talking about audits. We went into it with you in your 1952 hearings. I don't like to see you play down your own hearings because I thought it was a first class job. We prepared a great deal of material. It is in several volumes. I really think it is worth all of us rereading. I think it was a good job.

Representative PATMAN. We are very proud of it, Mr. Martin, but that was a very small part, the auditing was a very small part of it.

Mr. MARTIN. All of the questions were gone into. I give you credit for this. I can't remember a time when I have been up here that you have not raised this point. So I commend you for persistence and energy. But I don't think it is fair to say it has not been raised very carefully.

Representative PATMAN. I will keep on raising it until we have an audit by the General Accounting Office, Mr. Martin.

Mr. MARTIN. I have no objection to your raising anything indefinitely. I say sincerely—

Representative PATMAN. One other point and I will be through.

Mr. MARTIN. I want all members of the committee or any other committee of the Congress to raise all questions.

Representative PATMAN. You are very kind in giving us the benefit of your views, either in writing or orally, like you are now. You don't always furnish us everything that we want, but generally you furnish the information.

The other thing I asked you about is the manager of the account in the New York bank, and you said you had the power to stop his pay. In other words, stop his salary. The truth is, Mr. Martin, the Federal Reserve banks have the power to stop your salary, don't they? The only money you get you get in assessments from these 12 banks. Suppose they denied you?

Mr. MARTIN. We would complain to the Congress, Mr. Patman. I am sure you would protect us.

The CHAIRMAN. Senator Javits?

Senator JAVITS. Mr. Martin, this is the first time I have had the opportunity to question you.

I was very greatly interested in your testimony before the Housing Subcommittee the other day—I am a member of the Banking and Currency Committee—because of your views of the fact that there were relatively few parts of the housing bill that were inflationary. I think you emphasized the extension of the maturities of FHA guaranteed mortgages and the proposed reduction in downpayments as two such instances. But you did not include among inflationary things—I wish you would confirm this—urban renewal, or public housing as necessarily contributing to the inflation we are talking about in these hearings.

Am I correct?

Mr. MARTIN. I supported both the urban renewal and the public housing programs. I put my whole statement in the atmosphere of the present economic situation in which I said we were facing a dangerous psychological problem. Not being a technician on housing, as such, I did not purport to testify as a technician on the matter.

Senator JAVITS. That leads me to this question.

We have been doing a lot of discussing about the budget and exceeding the budget. I have been very disturbed about the fact that it has become a shibboleth. If you exceed the budget by a quarter, the whole world is going to collapse. Therefore, I would like to ask you whether in being concerned about the budget there is any selectivity, and if so, how should it be manifested?

What should we do about this budget?

Suppose you had to spend another billion dollars for some extremely constructive purpose—Congressman Curtis says highways, which may not necessarily be so—I just wondered whether in your own calculation in this thing there is any selectivity.

When one talks about breaking the budget, must you not qualify that by that you break it for in order to really know that you are contributing or not contributing to inflation?

Mr. MARTIN. I think there is and should be selectivity.

I remember in February, Senator, you questioned me along the line of whether the budget had to be balanced in a penny sense.

Senator JAVITS. Exactly.

Mr. MARTIN. I replied that it did not have to be in that sense. I think the emphasis since that time has shifted in the direction that it now should show a surplus. It is more essential that we take the position that Mr. Patman has espoused so vigorously this morning,

of recognizing that we are in good times and that we should be very selective about our expenditures, trying to get a little fat on our bones during the good times, paying down our debt a little bit and being in a strong position when the poorer times come.

Senator JAVITS. When we have good times, we can afford to pay taxes, too, can we not?

Mr. MARTIN. You have to pay taxes in either sense, but you have to pay for it whether in good times or bad times in one form or another.

Senator JAVITS. Hence the Congress, in your opinion, would have a responsibility to have an adequate tax burden in good times in order to do what the country needed done, and at the same time produce a budget surplus; is that not correct?

Mr. MARTIN. Yes.

I have repeatedly stated, and in the speech to which Senator Douglas was referring this morning before you came that I made last December, I tried to point out that this country—as a rich country in my judgment—can do the things that it is required to do, but it cannot do them unless it is willing to pay for them.

Senator JAVITS. Would you consider this 1½-cent increase in gasoline taxes as being a constructive measure at this time?

Mr. MARTIN. I definitely would.

I want to say, however, that I have not studied this or, as I have indicated, the highway program, as such. I am generally familiar with it recently; but I certainly would prefer raising taxes if I were doing it at the present time, granting the problems that Mr. Curtis mentioned. To that extent I was right alongside Mr. Patman.

Senator JAVITS. If you were going to do it at any time, this would be the time to do it, would it not?

Mr. MARTIN. That is correct.

Senator JAVITS. So we can realize a budget surplus not only by cutting down on expenditures which may be essential to the country, but we can also realize it by taxing ourselves in order to pay for the things that ought to be done.

Mr. MARTIN. I agree with that completely.

I think that you ought to close whatever tax loopholes there are and we ought to have a taxing program which would produce more revenue with more incentives for capital. That is a very easy statement to make but it is a very difficult thing to do.

Senator JAVITS. Yes. I am proud to say when I had an opportunity in the Senate to vote, I voted for the 1½-cent gasoline tax increase. I will again. I think it is in the interest of the people I represent.

I also voted with Senator Douglas to eliminate tax loopholes.

I think in this whole budget debate, we have begged the question of paying for what we get at a time when we can well afford to do it. At the same time we are beating ourselves over the head with an artificial standard—that is the budget—which was concocted and just has to stay this way no matter what the country has to do, especially to keep up with the Russians in this grim life and death struggle in which we are engaged, and which is a new factor that never appeared before when everybody was considering budget balancing to be some kind of religion.

There is nothing in this argument that has been going on with Congressman Reuss, as I understand it, to inhibit the Federal Reserve from at any time buying long-term bonds that it wants to.

Your testimony on the 27th is very clear on this. The Open Market Committee at any time can go out and buy long-term bonds, and you indicate that it does from time to time do so, even currently; is that correct?

Mr. MARTIN. That is correct, as we can do so at any time.

Senator JAVITS. You do not need any resolution or anything else in order to effectuate it?

Mr. MARTIN. That is correct.

Senator JAVITS. Your real problem is, is it not, to find some way of marketing long-term bonds at interest rates which bear a relation to the risk a person is taking in buying the bonds of the United States?

Mr. MARTIN. That is correct.

Senator JAVITS. Do you think that that risk that a person takes in buying bonds of the United States is adequately portrayed by the 4¾ percent interest rate which characterized the last long-term issue?

Mr. MARTIN. As of that moment, I don't think there was any alternative. I think we have denied the Treasury the tools which would have made it possible to have had lower interest rates if they had had some choice of how they might go to the market. As the largest borrower in the market, and a necessitous borrower, the Treasury is not, as some people think, in a position to make the market. They come to the market as a suppliant.

As long as the people find that the interest ceilings or the quotations in the market are such that they are put in a position that the only place they can deal is in the short end of the market, it is not surprising that the Government finds itself in difficulty.

I would just like to illustrate that as I did the other day when you were not here. I think it is a deplorable situation that the U.S. Government is in at the moment. That is if you as an individual—and this relates to this matter of long- and short-term security—have time payments coming due on your car and television set and you have charge accounts and you have not been able to save up any money, and you have a large mortgage on your house which, instead of being financed at 20 or 25 years, is coming due every 90 days, is it small wonder that under those circumstances that your creditors are going to be loath to be generous in their approach to financing?

Senator JAVITS. What are the tools that you want specifically which will enable you to do the job the way you ought to do it. You say we have denied you the tools.

Mr. MARTIN. I said the Treasury has been denied the tools of approaching the market as a bona fide customer and therefore has been put at the mercy of the market.

Senator JAVITS. In other words, the plea is to take off this interest rate ceiling?

Mr. MARTIN. That is right.

Senator JAVITS. Is the 2-year takeoff satisfactory?

Mr. MARTIN. The 2-year takeoff, in my judgment, makes it very difficult. You only have a 2-year period in which to test and then a new President and a new Secretary of the Treasury or the same Secretary of the Treasury will be faced with the same debate, and that will be a market influence.

I believe the level of savings in recent months has been sufficient to sell long-term Government bonds at lower than present interest rates

if we could convince people that the Government was going to have the flexibility to manage its finances soundly. We have not yet succeeded in convincing them.

Senator JAVITS. You agree with the insurance company economists who appeared before us the other day that one of the big lacks here is the fact that we are not selling an adequate amount of savings bonds to individual investors?

Mr. MARTIN. That is correct.

Senator JAVITS. Then why do you put a limit on yourself in your application to the Congress of 3.75 percent on those? Why do you not take the ceiling off savings bonds, too, and give yourself complete flexibility?

Mr. MARTIN. This is the Treasury bill. The Treasury bill did take it off. The Treasury is not limiting itself.

Senator JAVITS. In other words, you think it ought to be done?

Mr. MARTIN. I do.

Senator JAVITS. You ought to have a ceiling off both?

Mr. MARTIN. Yes, indeed.

I make the positive statement that the series E savings bond individual over a period of years has tended to be discriminated against and is the very person we ought to be showing the most concern for.

Senator JAVITS. Do you think that the United States in the savings bond effort is getting its fair share of the savings of the individual as contrasted with mutual banks, commercial banks, insurance companies, savings and loan associations, and other depositories of America's savings?

Mr. MARTIN. I don't know what the fair share is, but I don't think they are getting an adequate share.

Senator JAVITS. I think that answer is adequate.

Does the Federal Reserve have any figures on that subject to show just what we are getting and why we are not getting an adequate share?

Mr. MARTIN. I think the Secretary of Treasury's statement in the Ways and Means Committee hearing is a very good expression of that.

Senator JAVITS. We can get that.

You do agree with this fundamental proposition which I have put forward here myself? I was delighted to see these insurance company economists agree with it. That is, that this is a major area in which something effective can be done.

Do you think that it is a feasible alternative to the idea of some open market operation greater than now being undertaken by the Federal Reserve System?

Mr. MARTIN. I don't think it can be put in terms of alternatives. I think that in order to have as low interest rates as are warranted, we have got to follow sound monetary policies.

One of the points that I have tried unsuccessfully to make is that under present conditions an easing of money as such by the Federal Reserve would, in my judgment, further erode confidence in the dollar and lead to higher interest rates.

People find that difficult to understand. There have been references here to "metaphysics" in the field of money and credit, but confidence is the basic factor in money, and you can't get away from it. That is why it is so difficult to deal with.

Senator JAVITS. My time is almost up. With the chairman's permission, I would like to ask you two questions.

Do you feel that a greater sale of savings bonds to the public would strengthen confidence in this psychological consideration which you have spent some time developing?

Mr. MARTIN. Yes, I do.

Senator JAVITS. Your answer to that is "Yes"?

Mr. MARTIN. The answer is "Yes."

Senator JAVITS. To sell more savings bonds. That is a great factor in building confidence?

Mr. MARTIN. That is right.

Senator JAVITS. The other question I had was this:

Can anything be done with the rather large amount of Government bonds that are in trust fund accounts of the Federal Government?

We have figures here. They are very appreciable. I am sure you know them better than I do. Public debt obligations held by Government trust funds of a marketable character represented almost \$10 billion as of June 30, 1959, and, in special issues, about \$45 billion.

Is there anything which could be done in those funds to meet somewhat the views of people like our friend and colleague, Congressman Reuss, on purchasing long-term debt in the public market or selling when you choose? Has any consideration been given to that question in the Federal Government?

There is a tranche, to use a financial term, of bonds and a good deal of it in marketable debt. Can anything be done to use those funds in open market operations which will not run into the same difficulties which you people see in Congressman Reuss' other proposal?

Mr. MARTIN. The Treasury has the responsibility and authority for the administration of those funds. However, I think those funds should not be used for open market operations as such. They should be used for the soundest investments that the Treasury can make. I would not think that they should be used to attempt to influence the market as such.

Senator JAVITS. In other words, as trust funds they would not be available for that purpose?

Mr. MARTIN. That is right.

Senator JAVITS. Thank you, Mr. Chairman.

The CHAIRMAN. Congressman Reuss?

Representative REUSS. Mr. Martin, I want to start in where Chairman Douglas left off. To recapitulate your colloquy with the chairman, he said, "Look, Mr. Martin, you called the sense resolution 'printing press' money. Would you, Mr. Martin, tell us whether there is any difference between increasing bank reserves by lowering reserve requirements and achieving the same amount of increase by purchasing U.S. securities"?

Your answer was, "No, substantially there is no difference."

But you left just a little blip on the radar screen. You talked about a situation which might arise in a depression, when you would need to expand the monetary supply so far and so fast that you would feel handicapped by a recommendation that you do it just by purchasing U.S. securities, and therefore you would want to feel free to use the method of reducing reserve requirements.

Is that a fair statement of where the argument stands at the moment?

Mr. MARTIN. Not quite, Mr. Reuss.

I think I have never said we should use either one of these instrument alone. I have said that they both play a role. I have tried to go over this thing in the "mathematical" or "ultimate" sense. I don't think that the fact that it may come to an end or mathematical result has the same effect on what I call the flow of money. I think that this is where the elements of confidence and judgment come into monetary policy.

To go back again to your amendment, I don't see how it can be construed. I did not say that the amendment itself was printing-press money. I said that many thoughtful people would construe it as such in the light of the present circumstances in which we are dealing.

At the present time, the logic is more in terms of selling long-term bonds if we had them. Selling intermediate bonds, not purchasing them. Yet all the emphasis is put on the reverse.

Representative REUSS. I want to take you right back on the Douglas-Martin track now. If my ears did not deceive me, the only difference you were able to point out between the two methods of increasing bank reserves, and it is not necessary for me to repeat what they are since we are familiar with the two, was that in a depression you would not be able, you feared, to create money fast enough by relying solely on the purchase of U.S. securities. You wanted the ability to lower reserve requirements.

Let me ask the chairman is that correct. I am trying to recapitulate.

The CHAIRMAN. I have the transcript here.

Representative REUSS. This is just this morning.

The CHAIRMAN. That is my general understanding.

Mr. MARTIN. In a recession period is the only time we have been reducing reserves.

Representative REUSS. Your objection to the resolution of the Ways and Means Committee, which says that when you increase money, bank reserves, do so for the next 2 years by the purchase of securities rather than by a further lowering of bank reserve requirements, your objection to that as stated to Chairman Douglas a few moments ago was that this would unduly restrict you in a period of depression when you would not be able to move fast enough if all you could do was to buy U.S. securities. You would want to lower bank reserve requirements. Is that not a fair statement of what you said?

Mr. MARTIN. Let us change the word "depression" to "recession."

Representative REUSS. All right.

Mr. MARTIN. I think it would unduly restrict us right along.

We have this new bill that has been passed by the House and Senate and recently signed into law, and we have a lot of complications with the use of this instrument.

I just don't think, Mr. Reuss, that you can say that this is the only objection to it. I think what you are talking about is flexibility. As I pointed out to you, let us assume that we had a dramatic reverse and we had a terrific inflow of gold; I am sure we would use reserve requirements immediately.

Representative REUSS. You would use them on the upside. We are talking about on the downside. We are talking about increasing the money supply.

Mr. MARTIN. I am merely talking about flexibility, that is all.

Representative REUSS. This is going to take more time than I had hoped, but I must get my mind working with yours on this so that we can make a more intelligent record.

As I understand what you said to Senator Douglas, you said, "No, I can't go along with the Reuss sense resolution because that compels us for the next 2 years, when we are increasing the money supply, to do so by purchasing U.S. securities. This," you said, "reduces a flexibility which the Federal Reserve would like to have if there is a depression," and you corrected me to recession and I will accept the recession.

If there is a recession, we might have to increase the money supply so far and so fast that it would unduly restrict us to limit ourselves to the purchase of U.S. securities.

I am not getting very far toward getting you to agree with whether that is what you said or not, so let us let the record speak for itself as to whether you said that, and let us go on with the issue thus joined.

If that is an objection to the sense resolution, is it not rather odd to criticize the sense resolution on the ground that it smacks of printing-press money, when this particular objection which you raise to it is that it does not give you enough opportunity to create money, you want more?

Therefore, Mr. Mills, Mr. Rayburn, myself, Senator Douglas, and the other people who think there might be something to this resolution, far from being lovers of printing-press money, are less so than you are on this.

It seems to me that you are saying that this does not give you enough opportunity to expand money. Would you address yourself to that?

Mr. MARTIN. I can't address myself to it any more than I did in the letter which we have in the record. I did not accuse you or Senator Douglas or anyone else of being in favor of printing-press money. I said that thoughtful people would construe this resolution to mean that we were not going to handle our finances under present circumstances correctly but might resort to it.

Representative REUSS. Be that as it may, is it not a fact that in the current controversy raised by Senator Douglas' colloquy with you, it is you who are saying that you want more power to create money, to expand the money supply, than Senator Douglas, myself, and others are prepared to give you?

Mr. MARTIN. Let us put it this way: I am saying that under present conditions I think it would be a mistake to change the Federal Reserve Act. But if the Federal Reserve Act should be changed, it ought to be done directly as a part of that act and not as an amendment to a debt management bill.

Representative REUSS. That I do not think is particularly responsive. Let me go on.

In the next 2 years, with about \$18 billion in present bank reserves, and with the estimate of the economic situation which you have just given in answer to questions by Senator Javits and others; namely, that the problem is going to be an inflationary rather than a deflationary or depression problem, and with some \$63 billion of the public

debt in the hands of the banks—and you have repeatedly said that bank holdings of the public debt are bad, inflationary, and dangerous—do you seriously feel that it wouldn't be possible for the Federal Reserve to create any foreseeable needed additions to the money supply by purchase of U.S. securities?

Mr. MARTIN. No, and I have never said so.

Representative REUSS. That is fine. I am satisfied with that answer and I will not pursue it further.

It does seem to me to liquidate the point you just made to Senator Douglas.

Let me now ask you this: When asked why you do not use the device of raising bank reserve requirements, you have frequently said that this instrument is a blunt one and that is why you hesitate to use it. Is that not correct?

Mr. MARTIN. Yes. I have made that statement.

Representative REUSS. That it falls upon different banks with a different thrust, and hence you do not like to use it too much?

Mr. MARTIN. As I said when talking with Mr. Curtis here, I disagreed with him a little bit and I will write a paper of which I will send a copy to you, on the instrument.

The point I am trying to make on raising the reserve requirements is that if the demand for credit is active, as it is at the moment, let us say, and reserve requirements were raised to tighten money, in my judgment it would increase interest rates more and more abruptly than if open market operations were used. The reason is that we can't compel a bank to pull down its loans. They may be lending too much or too freely to customers. That is essentially a judgment that they make.

When we put up reserve requirements, they have to get the reserves and deposit them with us. They can get those reserves either by curtailing loans, which under present conditions they are not likely to do, or they can sell securities. If they have Government securities available, those will be the first they will sell. That means that pressure is put on the Government securities market and interest rates go up.

Two or three times proposals have come in to us that in order to tighten up on money, why don't we raise reserve requirements? In my judgment we would have knocked the spots off of the bond market if we had raised them under the prevailing conditions. That is a matter of judgment.

The CHAIRMAN. If the gentleman will yield to me for a minute, could not that difficulty be removed by a gradual increase in reserve requirements and not a sudden and sharp increase?

In other words, that the percentage would increase by one-half of 1 percent on a given date, three-quarters of 1 percent 2 weeks afterward, and so on, so that the full impact would not be immediate, but would be spread over a period of time?

Mr. MARTIN. We have used that approach to reserve requirement changes on occasion, Senator.

The CHAIRMAN. There would be no drastic application of brakes but merely a slowing down of the speed.

Mr. MARTIN. I don't think it would work that way at all. That depends on the demand conditions. We have used this spreading the

reserve. I don't think when the demand for credit is strong, as it is at the present time, you can.

The CHAIRMAN. You used it only in depressions or recessions, that is, the lowering of reserve requirements?

Mr. MARTIN. Since 1951, yes.

The CHAIRMAN. When you say "you," you mean the Board?

Mr. MARTIN. That is right.

Representative REUSS. Also, is it not true that the raising of reserve requirements could be accompanied by an equivalent purchase by the Federal Reserve of U.S. securities, so that the total effect on systemwide bank reserves was neutral?

Mr. MARTIN. You mean the total sale. You would not want to purchase them at the same time.

Representative REUSS. Yes, I would. Why would you not?

Mr. MARTIN. Why would we do it?

Representative REUSS. For the reasons that is so present in Senator Douglas' mind; because we would like to save some hundreds of millions to the taxpayers and cut Uncle Sam in for one-seventh, at least, of the benefits of the credit-creating power.

Mr. MARTIN. I question whether you would save these hundreds of millions.

Representative REUSS. The question was, however, whether a co-terminous purchase of U.S. securities could not in fact avoid the money-tightening effect of raising reserve requirements and leave the money supply in equilibrium.

Mr. MARTIN. We try to have as orderly a money market as we can and that sort of movement is not a good movement, to buy and sell simultaneously. That is not generally good unless you have a real objective and purpose on the money stream.

Representative REUSS. In this connection, the question of raising reserve requirements, the House Committee on Banking and Currency on May 28, in its report, asked the Federal Reserve to give study to the problem of making a useful monetary tool out of raising bank reserve requirements, and requested the Federal Reserve to report to the committee as soon as practical concerning possible improvements in the techniques of employing reserve requirements as an anti-inflationary tool, together with recommendations for any remedial

Representative REUSS. Because this development of useful anti-effect.

I trust you are working on that right now.

Mr. MARTIN. We are working on that right along.

Representative REUSS. Because this development of useful anti-inflationary tools I think is so important, I certainly hope you are not going to allow Congress to adjourn without making that report that the Banking and Currency Committee asked of you 2 months ago.

Mr. MARTIN. It depends on when Congress adjourns.

Representative REUSS. Assuming that we are here for another 2 weeks, I would certainly hope you would give us the benefit of your thinking.

Mr. MARTIN. I don't think we could have it finished in 2 weeks.

Representative REUSS. When do you think you can?

Mr. MARTIN. I don't know. We have a terrific volume of work. We are working on a lot of problems.

We will do the best we can.

Representative REUSS. Will you accept this sense of urgency on my part? I cannot imagine anything more important. When I look at some of the work on the inflation problem that is done in some branches of the administration, I really wish that the forces could be marshaled on this very important problem.

The Banking and Currency Committee needs some guidance, and we hope that you will give it to us as soon as possible.

Let me now turn to another matter.

The testimony of the Federal Reserve System before the Congress, just a couple of months ago in connection with the vault-cash bill, was very clear to the point that the Federal Reserve had not only used the method of lowering reserve requirements as its principal method of monetary expansion in the last 5 or 6 years, but that it intended to go right on using it. It intended to do so in the creation of the approximately 3 percent annual additions to the money supply, which the Acting Chairman envisaged would be brought about by further lowering of reserve requirements.

It was also stated very candidly, I thought that the reason for this was to enable banks to have more earning assets; in other words, make higher profits.

It was further stated that if this lowering of reserve requirements created too much money—I won't say printing press money—that then this could be sopped up by further selling U.S. securities from the portfolio of the Federal Reserve.

I think I have accurately stated the testimony of the Federal Reserve. If there is any doubt about it, I will be delighted to furnish page references for all of that.

Is that still your policy?

Mr. MARTIN. We don't have a fixed policy on that, Mr. Reuss. We don't have policies that we can put into print as such. We are meeting and considering the overall picture every 3 weeks in the Open Market Committee. Outside of what we publish, we don't have anything that is fixed as such.

Representative REUSS. We got the impression from all the testimony of the Federal Reserve people and from the staff study, that you are going to lower bank reserves. That is how you are going to add to the money supply, that everyone concedes is going to have to be increased over the years. Is that a wrong impression I have?

Mr. MARTIN. No. I have repeatedly testified here today and elsewhere that I think, generally speaking, bank reserve requirements have been higher than are necessary for the long-range development of the country.

The CHAIRMAN. Therefore, you believe that they should be lowered?

Mr. MARTIN. When appropriate, yes.

The CHAIRMAN. That is the impression I had.

Representative REUSS. Our impressions were right. I therefore think that the sense resolution we are talking about is not an unnecessary thing.

On a new subject, what is the extent to which wholesale price raises since January 1958 have been due to an excess of demand over supply.

Mr. MARTIN. They have gone up.

Representative REUSS. They have risen. The question is, Have they risen because there has been an excess of demand, or for some other reason?

Mr. MARTIN. I don't know what other factor is making them go up.

Representative REUSS. They have either risen from an excess of demand or for some other reason. Do you not have any opinion as to what caused them to rise?

Mr. MARTIN. I haven't made any exhaustive study of wholesale prices. Mr. Noyes may have some comment.

Mr. NOYES. Frankly, sir, I don't know what you have in mind.

Representative REUSS. What I have in mind is this: It seems to me quite extraordinary, frankly, that the Federal Reserve is unable to tell me if inflationary conditions have prevailed in the last 18 months.

My question is, Have these price increases occurred as a result of inflationary excess demand, or because of something like administered prices in these fields?

Mr. MARTIN. If you get into the field of administered prices, I just don't know. People are going to hold prices as long as they can.

Do you mean they are administering them up here?

Representative REUSS. It does seem to me that when you are administering a monetary policy, it would be well to know whether prices are rising because of an excess demand, which can be sopped up by a restrictive monetary policy, or whether they are rising for some other reason, in which case a restrictive monetary policy is not what the doctor should order.

Mr. MARTIN. I don't know all the commodities that go into this index, but I would say there has been pretty heavy competition on the price front in all of them. I see no reason to question that supply and demand has been a factor.

As to why people accumulate inventories or what their reasons for stocking up are, those are all factors that go into these things. I don't think we can have an accurate gage of the motives by which people acquire inventories or acquire commodities.

(Mr. Martin subsequently submitted the following for the record:)

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
OFFICE OF THE CHAIRMAN,
Washington, August 7, 1959.

HON. PAUL H. DOUGLAS,
Chairman, Joint Economic Committee,
Washington, D.C.

DEAR MR. CHAIRMAN: Enclosed is a copy of a letter which I am sending today to Congressman Reuss, together with a paper dealing with basic commodity price indexes in relation to price analysis.

It occurred to me that the paper might be of interest to you and probably to the other members of the committee.

Sincerely yours,

WM. MCC. MARTIN, JR.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
Washington, August 7, 1959.

HON. HENRY S. REUSS,
House of Representatives,
Washington, D.C.

DEAR MR. REUSS: In connection with my testimony before the Joint Economic Committee last Thursday, you asked me about forces affecting wholesale prices. It was not clear to me at the time exactly what aspects of this matter you had

in mind and wanted me to discuss. As you are no doubt aware, it is an extremely complex question, because any index of wholesale prices necessarily includes many different items which are subject to a host of different influences.

It so happens that one of the members of our staff has recently completed a very interesting analysis of basic commodity price movements in the recent period and, in view of your expressed interest in the subject, it occurred to me that you would like to have a copy. I am, therefore, enclosing, for your information, the paper prepared by Mr. Murray Altmann of our Division of Research and Statistics.

A copy of this letter and its enclosure is being sent to Chairman Douglas.

Sincerely yours,

WM. McC. MARTIN, Jr.

BASIC COMMODITY PRICE INDEXES IN RELATION TO PRICE ANALYSIS

(By Murray Altmann)

Since recovery from the 1957-58 recession began in the spring of 1958, prices of basic industrial commodities have generally advanced. Prices of basic foodstuffs, meanwhile, have generally declined. In consequence, most regularly compiled indexes of basic commodities have shown only small changes. This behavior very closely resembles developments in the first year of recovery from the 1953-54 recession.

Study of commodity-price developments can be very useful in cyclical analysis. As indicators of demand trends or of prospects for more comprehensive measures of prices, however, the basic commodity indexes are of questionable value. Furthermore, they make little if any contribution to an understanding of price-level changes over longer periods. A rationale of changes in price levels between two points widely separated in time requires study of the process of change in the intervening period—a study of the interaction of demand, cost, productivity, and price developments.

Most of the basic commodity indexes were developed many years ago when agriculture was a relatively larger part of the economy than now and when, prior to the modern type of Federal price support programs, prices of some agricultural commodities fluctuated more widely. Consequently agricultural commodities, mainly foodstuffs, have weights in these indexes which far exceed their current importance in commodity production and trade.

The emphasis on agricultural commodities, and the omission of such important industrial materials as lumber and fuels, also results partly from the requirement that the indexes be calculated daily. It would be accidental if a list of commodities chosen on this basis were representative of general commodity-price developments. The approach is indicated in the following quotation from a description of Moody's index, contained in "Commodity Price Indices," published in 1937 by the National Association of Purchasing Agents: "The number of commodities in the index was limited to 15 leading staples, to enable its prompt compilation daily, soon after the close of the various markets. Yet this limitation did not prevent the inclusion of practically all those raw products, dealt in on recognized central exchanges for futures and actuals, in which general day-to-day business and speculative interest is centered and which are commonly referred to in daily market reviews as 'commodities.'"

RECENT CHANGES IN BASIC COMMODITY PRICES AND PRICE INDEXES

The attached table shows price changes for commodities which, in various combinations, are generally included in basic commodity indexes, and for a few commodities, such as lumber and leather, which usually are not included. Of the 15 industrials, all but 3 have risen since the spring of last year, and 10 have increased 10 percent or more. On the other hand, every one of the nine foodstuffs in the table has declined, and decreases for five have exceeded 10 percent.

As a generalization, it might be said that shortrun analysis of demand trends—of requirements of materials for use and inventory in manufacturing—focuses on the industrial items. The foodstuffs as a group are more often subject to sharp changes in supply which are not directly related to current trends in demands and economic activity; the expansion in hog production and marketings taking place this year is an example. Moreover, changes in prices of some of the foodstuffs (and cotton as well) in recent years have been largely in

response to changes in Federal price support programs. These programs tend to limit advances in prices when demands expand or production declines as well as to limit price declines; the stocks accumulated in the process of supporting prices in years of large output become available at around support levels should demands expand sufficiently or should production be curtailed.

The table also shows changes for a few of the more familiar published indexes of basic commodities. The BLS daily index of 22 commodities has risen only 1 percent since the spring of last year when recovery began in the United States. This index is divided into raw industrials and foodstuffs, with the former having an influence in the total of somewhat more than half by virtue of the fact that it includes 13 of the 22 commodities. The rise of only 1 percent in the total occurred despite an average increase of 14 percent in the industrials as foodstuffs declined 14 percent.

Reuter's index has declined 1 percent since the spring of last year, and the recent level is the lowest since 1946. This index, which is often used as a measure of changes in world commodity prices, is a weighted average of 21 foodstuffs and industrial materials, but the weights are such that its movement is disproportionately influenced by wheat, sugar, and other foodstuffs. Among the nonfood commodities, cotton has the heaviest weight.

The Dow-Jones indexes have also declined since the spring of 1958. These are very like the Reuter's index in that cotton, wheat, and sugar have the heaviest weights of the 12 commodities included.

Moody's daily index has declined 4 percent in the same period. Eight of the 15 commodities included in this index are industrial, but among these are silver and silk—two commodities of much less importance currently than in prewar days. As in the Reuter's and Dow-Jones indexes, furthermore, wheat and cotton are heavily weighted. So also are hogs and sugar.

RECENT CHANGES IN SPECIAL GROUPINGS OF WHOLESALE PRICES

Special groupings of foods and foodstuffs and industrial commodities, within the framework of the BLS wholesale price index, have been calculated at the Federal Reserve since the 1930's. Further breakdowns of these groups have also been provided—the industrial into materials and finished products, and the foods and foodstuffs into livestock and products and crops and products. This year, a further breakdown of the industrial materials has been developed, based primarily on the responsiveness of prices to short-run shifts in demands; they are called sensitive materials and, for want of a better title, other materials. These two groups, shown in the middle panel of the accompanying chart, together with the two groups of finished products shown in the bottom panel, comprise all the industrial commodities in the wholesale price index.

The index of sensitive materials is broader in its coverage of industrial commodities than most basic commodity indexes. It includes ferrous and nonferrous scrap; refined nonferrous metals and mill products; rubber; hides and leather; textile fibers and intermediate products; lumber and plywood; waste-paper; and residual fuel oil. These items account for one-fourth of the weight of all industrial materials in the wholesale index. Monthly, rather than daily or weekly, calculation of the index made it possible to include many of these commodities. Since prices of many of the items are available weekly or daily, however, it is possible to make reasonably good current estimates when they are desired.

The fairly smooth cyclical pattern of the sensitive materials index is apparent on the chart. So also is the tendency of the other industrial materials group to lag during the last two expansions in activity and to show downward inflexibility in the last two recessions. Furthermore, while these indexes should not be used in any strict stage-of-manufacturing analysis, in combination with measures of capacity and output of materials they are useful for analysis of price pressures and prospects.

In 1954, for example, recovery in output of materials was preceded by an upturn in average prices of sensitive materials. Prices of steel scrap and nonferrous metals began to rise rapidly early in the second quarter, and rubber and lumber began to advance soon thereafter. After midyear, fuel oils turned up. Hides and leather declined further through 1954 but then turned up at the beginning of 1955. Textiles were generally stable through the period. By mid-1955, the price index for sensitive materials had increased 8 percent from the early 1954 low. By then also, total industrial output of materials had increased

about one-sixth from the low in the spring of 1954, to a level slightly above the previous high in mid-1953. Output of major materials averaged 90 percent of capacity, with the steel, aluminum, and cement industries even closer to capacity operations.

After mid-1955, as the chart shows, advances in prices became more widespread among industrial materials, prices of consumer goods began to rise, and what had been a moderate rate of increase in prices of producers' equipment became a very rapid rate. These developments followed midyear increases in wages and prices in the steel industry. Whether any of these developments can be singled out as causes and others as effects is questionable. Strong demands, rising costs, and advancing prices were influencing one another in an inflationary spiral.

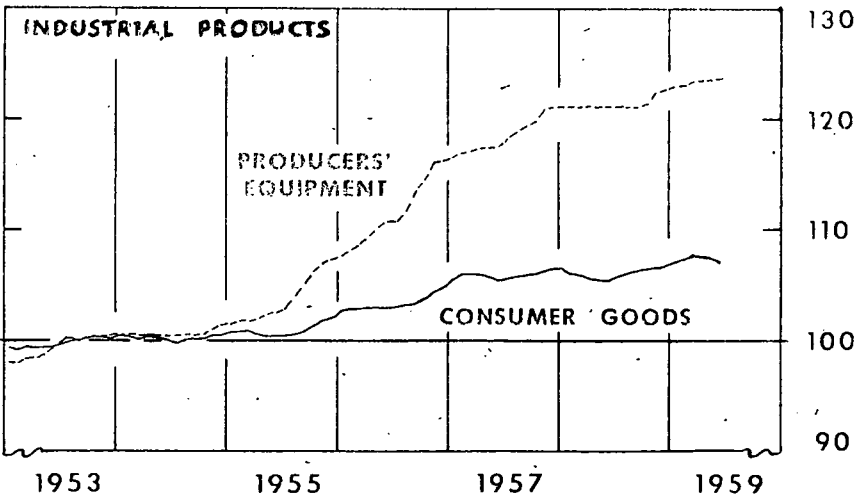
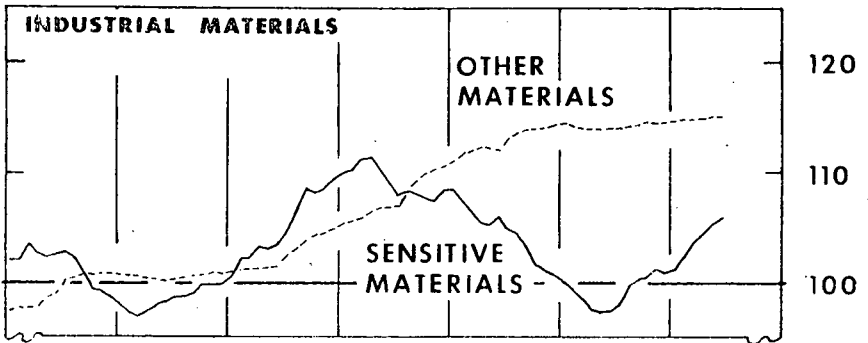
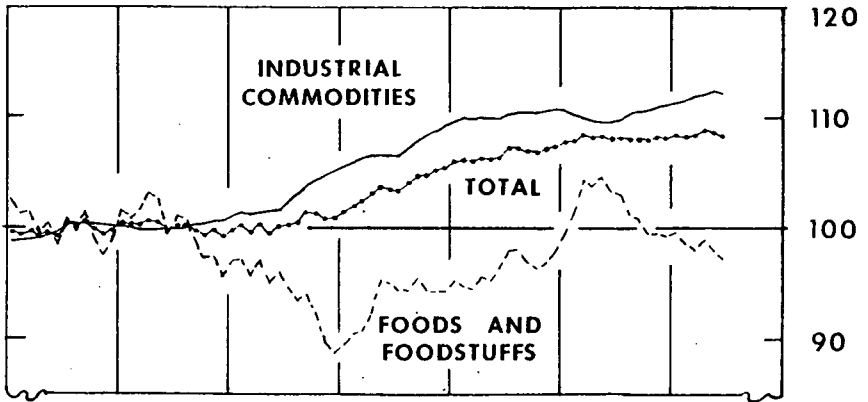
Since recovery in economic activity began in the spring of last year, the broad outline of price developments has been similar to 1954 and early 1955. Average prices of sensitive materials have advanced 9 percent. Metals, lumber, and rubber again turned up promptly. Nondurables have been much more prominent in the rise than in 1954-55, however, with hides and leather rising sharply through the period and textiles generally turning up this year. Average prices of other materials have been nearly stable, as during the comparable portion of the earlier expansion. The wholesale price behavior of consumer goods and of producers' equipment has also been similar to the earlier period. At midyear, furthermore, industrial output of materials was up more than one-fourth from early 1954 and was about 7 percent above peak levels in 1956 and 1957. Output of major materials was (prior to the steel strike) nearly 90 percent of January 1, 1959 capacity.

Prices of basic commodities

	Percent change—			Percent change—	
	Mid-July 1959 from mid-May 1958	Mid-May 1955 from mid-March 1954		Mid-July 1959 from mid-May 1958	Mid-May 1955 from mid-March 1954
Industrial:			Foodstuffs—continued		
Hides.....	99	-2	Steers.....	-6	-4
Wastepaper.....	65	10	Cows.....	-9	-2
Rubber.....	37	55	Wheat.....	-17	-2
Leather.....	32	-2	Cocoa.....	-23	-37
Copper.....	20	20	Sugar.....	-23	4
Steel scrap.....	20	47	Coffee.....	-26	-37
Print cloths.....	19	4	Hogs.....	-38	-30
Wool tops.....	16	-5			
Lumber.....	11	7	Indexes:		
Zinc.....	10	23	BLS daily.....	1	0
Tin.....	8	-3	Raw industrials..	14	10
Lead.....	3	-16	Foodstuffs.....	-14	-14
Cotton.....	-3	-1	Reuters.....	-1	0
Burlap.....	-4	4	Dow-Jones:		
Tallow.....	-20	-7	Spot.....	-6	-10
Foodstuffs:			Futures.....	-4	-14
Corn.....	-2	-4	Moody's.....	-4	-6
Cottonseed oil.....	-4	2			

WHOLESALE COMMODITY PRICES

1953 - 54 = 100



Representative REUSS. The next subject, consumer credit.

When did you come up with your report saying that no controls were needed over consumer credit? Was that about 2 years ago?

Mr. MARTIN. It was the spring of 1957, but I don't think we said "no controls." We came up with an exhaustive report on consumer credit and we have some inquiries continuing in that field.

We did not come up specifically and request controls. We had those controls taken away from us in 1952, as you remember.

Representative REUSS. Let me ask you to do this and submit it in time for the completion of this record here.

It does seem to me, from all I have heard from you, Secretary Anderson, and others, that we may well be getting into a period of real inflationary excess of demand. I would not think I was doing my duty as a Congressman, and particularly as a member of the Banking and Currency Committee, if I did not have the benefit of the judgment of the Federal Reserve System as to whether the controls over the amount of downpayment and length of maturity of consumer installment credit may not now be necessary.

I say this in recognition of what has been said about excess demand for goods, and in recognition also of what has been said about excess demand for savings.

Certainly, if you could cut down on the demand for credit by installment sales somewhat, you would make a little happier, it seems to me, the market for short-term Government securities.

Would you, therefore, file, at your convenience, but as soon as you can, a report on this with the Joint Economic Committee, so it will be included in our record?

Mr. MARTIN. I will be very glad to.

(Mr. Martin subsequently submitted the following for the record:)

An important factor in the heavy demand for credit which has generally characterized the postwar period has been the use of credit by consumers. This has included, on the one hand, short- and intermediate-term credit, such as charge accounts and installment credit and, on the other, long-term credit in connection with home mortgages. Since 1946 short- and intermediate-term credit has increased \$33 billion to a total of \$47 billion on June 30, 1959, and long-term mortgage loans to consumers, associated almost entirely with the purchase of homes for their own use, have risen by almost \$100 to \$117 billion as of June 30.

Whether the growth of this credit should be subjected to some form of selective restraint is a complex question involving judgments as to equity and administrative feasibility, as well as monetary policy. However, there is little question but that restrictive regulation of the terms offered to installment and mortgage borrowers would effectively reduce the total demand for credit and thus relax somewhat the upward pressure on interest rates. Conversely, it is also certainly true that the liberalization of terms, both as to downpayments and maturities, which has taken place since 1952 has contributed to the demand for credit and the upward pressure on rates in the recent period. This liberalization and expansion has been the result of the competition among private consumer lenders and installment vendors, in the case of short and intermediate credit, while in the case of long-term credit the Federal Government itself has taken the lead in promoting progressively lower and lower downpayments and longer and longer maturities on real-estate loans.

As indicated above, the selective regulation of the use of credit by consumers raises many problems beyond those implied in the general restraint of credit-financed demands. Such regulation has been vigorously opposed by interested groups whenever it has been proposed. After weighing the many conflicting arguments enumerated in the study submitted by the Board in 1957 (see pt. I, vol. I, ch. 16), the Congress may determine that the balance favors establishment

of permanent authority to regulate consumer credit. To be fully effective, such authority would have to cover long- as well as short- and intermediate-term credit and should be permanent, broad, and flexible in character. Application of the regulations should be limited to periods when the need is sufficient to justify the considerable burden such regulation imposes on the businesses directly affected and toleration of the discriminatory aspects which are unavoidable.

The Board does not feel justified, at this time, in taking the initiative in a recommendation to Congress in this matter. The effectiveness and workability of this kind of selective regulation depends heavily on broadly based acceptance and support. Whether such support exists can best be determined in the forums of the Congress itself.

The CHAIRMAN. May I amplify that?

As I see the movement in wholesale prices since 1955, the increases have primarily taken place in the field of construction and producers' durables, not in the field of consumers' goods, that is, soft goods. I would appreciate if in this report or reply which you make you indicate how in your judgment a restrictive credit policy confined almost exclusively to the short-term Government market by raising interest rates on short-term Government securities, would appreciably dampen down the price increases in these particular fields; namely, the fields where they have occurred.

You will get a copy of the transcript and I think the full nature of this request will be evident to your staff.

(Mr. Martin subsequently submitted the following for the record:)

It should be pointed out first that it is not, and has not been, the policy of the Federal Reserve System to "raise interest rates on short-term Government securities." The System's policies are directed toward the availability of bank reserves and are designed, in boom periods, to limit the availability of such reserves to the extent necessary to avoid an inflationary expansion of bank credit. In these circumstances, the resulting interest rates reflect the balance of private demands for and supplies of saving in the money and capital markets.

Relative movements of prices in free markets serve the classical economic function of guiding production, shifting resources and directing them into their most efficient use. The concentration of price increases among construction materials and producer durable goods in the 1955-57 period, to a large extent, represents the composition of demands that characterize an investment boom.

The Federal Reserve should not, and does not, attempt to control relative prices; its concern is with the overall price level. The way in which the Federal Reserve supplies or absorbs reserves can have a number of important effects, but it does not have a differential effect on specific prices.

Representative CURTIS. Mr. Chairman, that is one of the points I was going to make on Congressman Reuss' comments on increase in wholesale prices. That is, there is quite a mix. There are a number going up but some are not. Some are going down.

Just as you are pointing out, it is a mix over the long range. I think that bears on the matter. If it were a general across-the-board thing, we would have a different problem.

Representative COFFIN. I wonder, Mr. Chairman, if you could give us 10 minutes to answer a rollcall and come back?

The CHAIRMAN. We have a meeting of the committee in which the staff is going to report on the inflation study at 12:30. By all means go, and let us do that.

Representative COFFIN. I have a few questions I would like to ask.

Representative CURTIS. All I wanted to do was to post something in the record and then I will run along, if I may. That is on this highway thing, to get it away from the specific highway but to try to get it back to economics.

I am very disturbed at your answer. I am afraid it may be taken out of context.

The problem as I see it is that we are \$3 billion short in money in anticipated revenues for the next 3 years to meet the present highway act authority to spend. \$250 million of that is actually under contract. \$1.5 billion of this is in the hands of allotments of the States and is ready for imminent contract.

As I see it, there are four things that could be done:

1. Do nothing;
2. Use general revenue, which would add to the deficit or take from whatever surplus;
3. New taxes, in the context of the present tremendous taxload;
4. The short-term revenues tied to the trust fund;
5. The alternatives coupled with these possibilities of cutting back the program.

Actually, expenditure rate for these 3 years will be anticipated to be about \$3 billion a year, or \$9 billion. A cutting back would be to an expenditure rate of \$2 billion, which would mean \$6 billion.

What has happened by this bill is giving an additional \$1 billion and a cutback of \$2 billion. Of those four alternatives, I suppose the first one would be the least inflationary, although the economic damage that would result from the Government defaulting on \$250 million, plus a cutback on the anticipated contracts to be let on this big industry, I do not know.

The real question would be, which of the three methods would be the least inflationary: General revenue, which is deficit, or of surplus, the new taxes?

I presume that new taxes would be less inflationary, but I think that it is glib to answer too quickly when we have the difficult tax structure we have today.

Then the short-term revenues, if you would care to answer that for the record, or right now. On that standpoint I would think you would have to reserve your question of whether or not the bill itself, which cuts back expenditure rate by \$2 billion at least, is in total effect inflationary, in this context.

Mr. MARTIN. I will give you an answer for the record.

(Mr. Martin subsequently submitted the following for the record:)

It is difficult to point to a particular program of Government expenditure as being inflationary. It is the whole balance of Government revenue and expenditure which contributes to inflation or its restraint. The budget for 1960 promises at best a narrow and precarious balance or perhaps a small deficit. A substantial budget surplus, during a period when economic activity and private expenditures are rising so rapidly, would certainly be preferable.

The Ways and Means Committee announced on July 29 that it had agreed to the issue of up to \$1 billion in revenue bonds prior to June 30, 1961, to finance the prospective deficit in the highway trust fund under existing legislation and to the transfer beginning July 1, 1961, of 2 percentage points of the excise tax on passenger automobiles or about \$250 million per year to the highway trust fund. The committee has also recommended to the Public Works Committee of the House a stretchout in the program of highway construction.¹

¹ The Ways and Means Committee has subsequently revised its recommendation with respect to this matter to include a 1-cent increase in the gasoline tax. It should be noted that the following analysis relates to the proposal that was current at the time of these hearings.

There are difficult questions involved here as to the rate at which highways ought to be built and the means by which they should be financed. For the most part these are outside the area of competence of the Federal Reserve System. The least inflationary method of financing highway expenditures would, of course, be by increased taxes of one sort or another. This recommendation by the Ways and Means Committee would not provide any additional net revenue to meet the cost of highway construction, but would merely shift some general revenue to the highway trust fund and bridge a financial gap that would exist until highway construction activity is slowed down.

Although the revenue bonds which the recommendation contemplates would not be part of the public debt and would not be guaranteed by the U.S. Government, they would constitute additional borrowing that would be added to the sums to be borrowed for other Government purposes during the next year or two. As such, this additional borrowing would put further strain on the ability of the capital market to absorb both Government obligations and private issues and cause upward pressure on interest rates. Certainly the proposal to finance highway construction by the issue of revenue bonds would be more inflationary than financing this construction out of higher taxes.

Representative CURTIS. I would like to know what we should do here.

The CHAIRMAN. I might perhaps save some time if we revert to the points which I was dealing with which you partially touched on with Congressman Reuss. I was primarily discussing how the long-time secular growth in production could be financed by roughly corresponding growth in commercial funding.

The difference in our views became fairly apparent. I was urging that this would be done through open market operations compared to the purchase of Government securities. This among other factors would give increased revenue to the Federal and to the Treasury.

You advocated lower reserve requirements because you thought the present rates were too high.

If I may turn from this problem of secular growth to cyclical stabilization, I think the policy of the Federal during the fifties has been that during a period of recession you lowered the reserve requirements. During a period of boom, you raise the interest rates and sell securities.

Mr. MARTIN. Let me just interject—not alone.

The CHAIRMAN. Pardon.

Mr. MARTIN. Not just that alone. We have done both during the period. But the emphasis has been that.

The CHAIRMAN. In general, in a period of recession you lower reserve requirements.

Mr. MARTIN. And bought securities.

The CHAIRMAN. And during a period of boom you raise interest rates and sell securities?

Mr. MARTIN. No, the point I am trying to make is this: We didn't just generally in a period of recession lower reserve requirements. We also bought securities.

The CHAIRMAN. All right, I will come to that. But the main expansion during a period of recess has been what I have said.

Mr. MARTIN. I will give you a table on that.

The CHAIRMAN. I think you increased lending capacity of the banks by approximately \$3 billion through your decrease in reserve requirements. This has been done almost completely during the recession period.

My total is 4.1 billion, including time deposits. Excluding time deposits, it is approximately 3.7 billion.

Mr. MARTIN. I have a table here I would be glad to put in the record.

The CHAIRMAN. We would be very glad to have you.

Would you say whether this statement of mine is approximately accurate insofar as the figures are concerned?

Mr. MARTIN. Approximately, yes. There are some minor differences.

The CHAIRMAN. Yes, I understand.
(Information referred to follows:)

[In billions of dollars]

Period	Reserves supplied by open market operations	Reserves supplied by reserve requirement reductions
For the entire period 1952-1959.....	14.2	4.3
During the 1953-54 recession (May 1953-August 1954).....	0	2.8
During the 1957-58 recession (October 1957-July 1958).....	2.1	1.5

¹ For the entire period net reserves provided by open market operations exceed reserves provided during the 2 recession periods because purchases of \$2,100,000,000 were made outside the recession periods. The reserves supplied by reduced requirements add to the total for the entire period because the only changes during the period occurred in the 2 recessions.

The CHAIRMAN. Here is one difficulty which I noticed in the 1930's. I am not certain it applies in the 1950's. I noticed it in the 1930's very markedly. The banks had tremendous excess reserves. The mere creation of additional reserves for them did not cause them to expand their loans. Hence monetary policy was relatively ineffective during the depression period.

I do not use the word "recession." I say "depression" because that certainly was a depression. I am not certain you have had this same problem in the fifties. If the banks have excess reserves in a period of recession due to the fact that they decided not to loan as much and the volume of bank loans have diminished, would you be helping the situation any by lowering the reserves² and hence increasing their excess reserves?

Might it not be better if instead you went into the open market and bought Government securities because at least that would have the effect of raising the price of bonds and hence lowering yields, consequently lowering interest rates and consequently stimulating investment? I do not say "savings"; I say "investment."

Therefore, may not even your cyclical policy be wrong, namely, that in a period of recession, instead of using the chief emphasis, if you want to expand credit, upon lowering reserve requirements, might it not be wiser to buy Government securities, and in a period of boom, instead of selling securities you should raise reserve requirements gradually, and I do not say catastrophically.

Mr. MARTIN. It is flexibility that is needed. Senator. Flexibility is the approach. Under certain conditions we have to use both of them. That is exactly the way it has to be approached.

I don't think that the period of the thirties and the period of the fifties are at all comparable, and you don't either, of course.

In 1957 and 1958, a combination of open market purchases and lowered reserve requirements had a very dramatic impact on loans and investments of the banking system. The two will do the same thing and they must be used flexibly.

The CHAIRMAN. I want to come back to this question of who makes the earnings or in what proportion the earnings are divided.

As I see it, your policy of lowering reserve requirements naturally increases bank earnings. The policy of selling securities diminishes the interest yield which the Reserve banks make.

Mr. MARTIN. Let me tackle this earning thing for a moment.

I would like to see the banks, generally speaking, have assets on which they could earn money and—

The CHAIRMAN. I am not proposing to starve them. The question is whether their returns are excessively low at present. I would suggest that the alternative policy which I have suggested, namely, that if you do want to loosen credit in a period of recession, it could be done by buying Government securities which would certainly increase the earnings of the reserve banks and hence the Government.

If you raise reserve requirements in a period of boom, this would have a longrun effect of increasing the earnings of the Fed and hence of the Government. As I see it, one would be just as good as the other from a cyclical standpoint, but the advantage both from the standpoint of secular growth and cyclical control might seem to lie in the policy which I have suggested rather than in the policy which in the main you followed.

I simply took this time, Congressman, in your absence, and I would say Mr. Martin should have a right to make a considered reply to what I have said, but it is your turn now.

Representative COFFIN. Thank you, Mr. Chairman.

I have, first of all, just one correction in a document which I believe you have, Mr. Martin, on calculating the impact of Federal Reserve purchases of Treasury securities on Treasury interest costs.

Item (i) on page 2 has a minor error. The figure of savings in the 10th year is said to be in excess of \$80 billion and it should be \$80 million. It is not much of an error, only \$79,920 million, but I thought I would correct the error.

There has been, I understand, quite a lot of discussion this morning on the proper course for the Federal Reserve in combating cyclical changes as distinguished from reacting to a long-term secular trend. I do not want to repeat what has been said, but I am going to ask a question with the hope that it will produce a summary answer. You can either answer now or submit it for the record. This is the question:

What differences in techniques exist between raising or lowering money supply to counteract cyclical changes and raising the money supply in relation to long-range secular growth? Are there differences?

If there are, would you divide your answer into three points:

First, procedures to increase money supply to combat cyclical recession;

Second, procedures to restrict money supply to combat cyclical booms;

Third, procedure to increase money supply to keep up with the secular growth.

Can you answer that in reasonable short compass now?

Mr. MARTIN. I would rather have time to look at that and answer it in writing, if I could.

Representative COFFIN. I think this perhaps will repeat some of the discussion, but I do not think it has been brought into sharp focus.

Mr. MARTIN. I would like an opportunity to do it on paper, if I could.

(Mr. Martin subsequently submitted the following to the record:)

Representative COFFIN. What differences in techniques exist between raising or lowering money supply to counteract cyclical changes and raising the money supply in relation to long-range secular growth? Are there differences?

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Representative COFFIN. I think this perhaps will repeat some of the discussion, but I do not think it has been brought into sharp focus.

ANSWER

The Federal Reserve System has three major instruments available to it in determining the availability and cost of member bank reserves, thereby affecting bank credit and the money supply. These instruments are used in an interrelated manner in pursuit of the ultimate policy objectives of counteracting inflation and deflation and promoting steady economic growth.

Although counteracting cyclical movements and fostering economic growth may be regarded as separate objectives of monetary policy, these objectives are not pursued independently. The System does not at one time counteract the cycle and at another time act to encourage growth. Nor does it use one instrument or technique for anticyclical purposes and another to provide the monetary basis for growth. In other words, in using the instruments at its command, the Federal Reserve is always guided by both short-term and long-term considerations.

Although actions to offset cyclical tendencies and to encourage growth are not separable, it may be found useful to set forth some of the considerations that guide the system in the use of its instruments in pursuit of these goals. It should be noted, however, that the particular combination in which the three major instruments are used is likely to vary with circumstances. While we may divide economic history into periods of prosperity and recession for analytical purposes, the problems that arise at any point of time are always unique in some respects. Decisions as to the combination of instruments appropriate to the current situation are always ad hoc decisions—they are not and cannot be predetermined by any set of rules. Furthermore, Congress has wisely placed the responsibility for these decisions in a group of men, rather than in any single individual. Some decisions rest with the Board of Governors, some with the Federal Open Market Committee, and some are shared between the Boards of Directors of the Reserve banks and the Board of Governors. Among the men involved in these groups there are, and should be, differing views.

I shall confine my discussion to the three major instruments: open market operations, discount operations, and reserve requirements. The Federal Reserve presently also has authority to prescribe margin requirements on stock market credit but this special purpose instrument is not utilized for the purpose of influencing total bank credit and the money supply. I shall, therefore, not cover it in this answer. At times in the past the Federal Reserve has also been authorized to prescribe downpayments and maturities with respect to consumer installment credit and real estate credit. Since such authority does not exist at present I shall also not cover this type of instrument.¹

¹ In my accompanying reply to a question from Representative Reuss I have set forth some of the considerations with regard to whether or not such authority should be reestablished.

Actions in periods of recession

First, without respect to their relative merits, open market purchases, lower discount rates, and lower reserve requirements would be appropriate to combat a cyclical recession. All of these actions, if they are timed appropriately, should be conducive to increased investment and to an increase in the money supply.

There appears to be general agreement that open market policy should be shifted, first to lessened restraint and then to active ease if the recessive forces continue. Paralleling reductions in the discount rate as the level of market rates adjusts downward are also widely accepted as appropriate. As reserves are supplied through open market operations, member banks may be expected to reduce their indebtedness to the Reserve banks, and this relaxes one of the restraints on credit expansion appropriate to a boom period.

Some economists have argued that it is desirable to put a floor under the discount rate: i.e., to refrain from reducing it at some level even though market rates fall below that level. They base this argument primarily on the reasoning that a very low discount rate is not needed when reserves are plentiful, and that changes in the discount rate over a narrower range may help, at least psychologically, to lessen the range of rate fluctuation both ways. Others would contend that the widest possible fluctuation both ways is desirable in order for monetary policy to make its maximum contribution to general economic stability.

Agreement has also been general, until quite recently at least, that bank reserve requirements should be lowered and that, in fact, this was the most potent weapon in the Federal Reserve's arsenal of antirecessionary policy actions. This assumes, of course, that the prerecession level of requirements was high enough to permit a reduction without impairing their effective use as a fulcrum for monetary policy.

So far as I am aware, no one has questioned the effectiveness of reserve requirement reductions, or the fact that they have an important advantage over the other general instruments in a recession. Decreased reserve requirements affect all banks immediately and place every bank in the country under simultaneously pressure to lend or invest in order to maximize its earnings, whereas open market purchases have less immediate impact on many country banks.

Recent questions as to the desirability of using reserve requirement reductions to combat an economic downturn appear to be based on the ground that such action is difficult to reverse during periods of boom. This point has some validity and the limitations on the use of reserve requirement increases in periods of prosperity will be discussed in the next part of this answer. To the extent that such limitations exist, it would probably not be desirable ever to carry reductions below levels which would be appropriate from a longrun point of view.

To summarize at this point, all of the instruments of general policy may be appropriate to a downturn, depending upon its severity. The only limitation might be that reserve requirements should not be reduced below levels appropriate to longer run needs.

Actions in boom periods

Theoretically, all the same instruments are available to restrict growth in bank credit and the money supply in boom periods as are available to encourage monetary expansion in recession. There are, however, a number of significant differences. One difference stems from the fact that the problem in a boom is seldom one of literally contracting the monetary base, but rather one of restricting its expansion. Hence, unless redundant excess reserves remain from the preceding period of ease or there is a substantial inflow of reserves from other sources, a restrictive policy does not require that bank reserves be absorbed but simply that they be held stable or allowed to increase at a slower rate.

Open market operations are, generally speaking, the most quickly and easily reversible of all the instruments. In a period when restrictive monetary policy is appropriate, open market operations are likely to be utilized in a way that requires member banks to obtain a portion of the reserves to support monetary expansion by borrowing at the discount windows at the Reserve banks.

While there is considerable difference of view on the timing and amount of increases in discount rates, so far as I know there would be almost complete agreement that these rates at the various Federal Reserve banks should be moved up, as the general structure of interest rates responds to the increased demand pressures that develop in a boom period. Much has been written on the effectiveness of such action by the central bank, here and abroad. Some

observers give much greater significance to discount rate changes than others, but there would be almost universal agreement that increases are appropriate in boom periods.

Reserve requirement increases raise a number of problems. As pointed out above, the objective of monetary policy in a boom is not to reduce the monetary base and force credit contraction, but to hold expansion within sustainable limits. Hence, a boom, per se, would not call for increased reserve requirements unless a large volume of excess reserves remained from the preceding recession or were appearing from other sources; e.g., a sustained gold inflow. While such an operation presents extremely delicate problems of timing, excess reserves left over from a period of monetary ease should be absorbed early in the recovery, before a boom develops.

A difficulty in the application of reserve requirement increases is that their effects are large and pervasive.² In a recession, a substantial, pervasive impact may be all to the good, but even in the most thoroughly diffused boom, the shock of a general increase in reserve requirements would be likely to produce undesirable effects in many areas.

With reserve requirements at their present levels, which are high by longrun historical standards, and with the substantial outflow of gold that has been taking place, increasing reserve requirements has not recently been a pressing practical question. However, the Board has under study techniques for reserve requirement adjustment, both in connection with implementation of the authority contained in Public Law 86-114, and in response to a request contained in the report of the House Banking and Currency Committee on S. 1120 that the Board explore possible improvements in the techniques of employing reserve requirements as an anti-inflationary tool.

Summarizing the action appropriate to restraint in a boom period, it might be said first that restraint on monetary expansion is always the most difficult and controversial phase of monetary management, in this country and elsewhere in the world. This is due in large part to the inescapable fact that restraint is unpopular. No possible combination of monetary instruments can ever overcome the "spoil sport" role in which the monetary authorities are inevitably cast in periods of advanced recovery and boom. People whose expenditure plans are adversely affected feel that the restraint discriminates against them. Those who go ahead, and who preempt the needed funds by bidding a higher rate of interest may also complain. Bankers and other institutional lenders, although presumed by many to enjoy benefits from a restrictive policy, themselves become concerned about declines in the market value of outstanding securities they hold, and about their inability to make all of the loans they feel they could profitably undertake.

What the monetary authorities can do or should do, in the circumstances, is to center their policy around two objectives: (1) To hold monetary growth to a noninflationary rate; and (2) to avoid actions which might precipitate a crisis by tightening credit too quickly or which would distort the flow of credit and interfere with the free functioning of the allocative processes of the money and capital markets. To the extent that it is possible to generalize, this can usually be best accomplished by carefully conceived and conducted operations in the System's open market account, and appropriate upward adjustments in the discount rate. These may need to be supplemented by reserve requirement increases in some circumstances.

Provision for long-term growth

As noted earlier, increases in the money supply to accommodate and facilitate secular growth in the economy are not generally associated with specific instruments of policy. The amount of additional reserves needed to provide for secular expansion of the money supply in any year is relatively small, compared to the amounts involved in either seasonal or anticyclical operations. Thus, the growth needs of the economy would generally be met by withdrawing less reserves or by supplying more than seasonal or cyclical factors would otherwise indicate. The choice of instruments would be largely determined by the seasonal or cyclical situation prevailing at the time.

It might be noted in passing at this point that the question does not specifically refer to the use of the tools of monetary policy to effect seasonal adjust-

² A technical comparison of reserve requirement changes and open-market operations is contained in the accompanying answer to a question by Representative Curtis.

ments. The volume of transactions entered into for this purpose, both in the open-market account and through discounts for member banks, sometimes reaches very large magnitudes. Hence, the selection of the appropriate instrument for either secular or cyclical purposes may be considerably influenced by the seasonal situation. Furthermore, substantial relaxation or tightening of monetary policy may be accomplished by not acting to offset the reserve effects of seasonal movements, rather than by positive action. For example, in January, when there is always a substantial return flow of currency to the banks, there would be an easing of reserve positions to the extent that the System did not sell securities to absorb reserves. Similarly, a tightening in reserve positions can be brought about to the extent that a seasonal outflow of currency or deposit expansion is not fully offset by System actions to supply reserves.

Over a long period, our gold stock has increased, supplying reserves to the banking system and providing part of the basis for expansion of the money supply. On the other hand, in a growing economy, an increasing amount of cash is needed to carry on normal business. To the extent that currency in circulation expands to meet these needs, it operates as a drain on bank reserves. Over the long run, the relative size of these two magnitudes—gold, and currency in circulation—which are not normally subject to direct control by the monetary authority, will determine how much, if any, additional reserves need to be supplied to provide for growth in the total money supply. In some circumstances, providing the appropriate money supply for economic growth would be accomplished by the absorption rather than the expansion of reserves through monetary action, if, for example, gold were flowing in rapidly and currency in circulation were not increasing rapidly.

If we make the assumption that over the long run the increase in the monetary gold stock will roughly equal the increase in currency in circulation, as it has in the last 30 years or so, then it follows that the monetary authority should provide sufficient reserves in the course of its operations to permit an appropriate rate of growth in the demand-deposit component of the money supply. This can be done either by allowing Federal Reserve credit outstanding to increase gradually over time, or by reducing the percentage of reserves member banks are required to hold.

One of the considerations governing the choice between these alternatives is the long-run soundness of the financial structure. Long-term growth in the demand-deposit component of the money supply requires not only an adequate supply of reserves to the banking system, but also provision for an adequate capital structure. If deposits and risk assets grow more rapidly than the capital accounts, this gradually undermines the protection against loss that these capital accounts provide, first to the depositors, and second to the Government, the insurer of deposits through the FDIC. The ratio of capital to liabilities and risk assets in the banking system will not be affected much, one way or the other, by monetary policy actions in the short run. In the longer run, however, the level of reserve requirements, along with many other factors, will play a part in determining the rate at which banks are able to add to their capital, either by retained earnings or the attraction of new investment. The level of reserve requirements that member banks are required to hold with the Federal Reserve will also affect, in the long run, the attractiveness of membership in the Federal Reserve System, and national chartering as against State chartering, in the case of both existing and newly formed banks. These considerations are matters of concern, not only to the Federal Reserve, as a monetary authority, but to it and other Federal and State bank supervisory authorities.

Other things being equal, relatively high reserve requirements, by freezing funds most banks otherwise could use for loans and investments, would tend to result in lower earnings for the commercial banks and a smaller rate of return on the capital invested in banking—and relatively lower reserve requirements, by permitting banks to use more of their funds for loans and investments, would permit higher earnings and a larger rate of return on invested capital. Conversely, the earnings of the Federal Reserve would tend to be higher, if reserve requirements were high, and lower if they were low—again assuming other things to be equal. These matters are of concern to the monetary authority only to the extent that they affect the soundness of the financial structure and its ability to respond constructively to changing economic conditions and to play its role in overall growth effectively. The financial structure includes, of course, not only the commercial banks but also the Federal Reserve System itself and the nonbank financial institutions.

No objective indicator of the appropriate long-run level of reserve requirements is available. Ultimately, as in so many things, there is no choice but to entrust the responsibility for decision in this area to the hands of some human being or group of human beings, whom we admonish to use their best judgment in the public interest. At present this authority is vested in the Board of Governors of the Federal Reserve System, with respect to banks that are a members of the System.

This is an area in which it is not only possible, but desirable, for Congress to set an appropriate range within which the monetary authority should operate. The Congress has done this throughout the history of the Federal Reserve System and, as you know, made some modifications in the limits and bases with respect to reserve requirements in the current session. While some of the changes made by the Congress were not in accord with the recommendations of the Board, the limits prescribed in the Federal Reserve Act, as amended (roughly between 10 and 22 percent), appear to be reasonable and equitable, and the reserve requirements which the Board may specify from time to time, within those limits, should serve the immediate needs of monetary policy and provide for the continued sound growth of the financial system, which is one essential part of overall economic growth.

Depending on developments—including gold flows, the currency demands of the public, and many other factors—Government security holdings of the Federal Reserve System may increase or decrease, on balance, and its earnings and payments to the Treasury will vary accordingly. This incidental effect of the policies selected to make the maximum possible contribution to economic stability and growth should not, in our judgment, play any significant part in judgments as to the balancing of the instruments in either the short or long run.

Representative COFFIN. The second question is: In the boom of 1955-57 our policy was to dampen the boom. In 1957 and 1958, monetary policy appears aimed at stopping the rapid decline in business fixed investment. If we assume that changes in the supply of money and interest rates will affect the levels of investment, could not the Federal Reserve bring about the desired results more quickly and with less use of funds by operating directly in the long end of the market than by confining operations to the short end of the market?

I ask this because of the fact that the long end of the market is thin in the sense that relatively smaller operations, both in buying and selling, exert a greater influence.

The second part of the question is: Would not this practice of increased use of the long end of the market in a recession reduce the amount of liquidity you create and hence reduce the subsequent problems you face to prevent inflation growing out of recession-created liquidity or the overhang of liquidity?

In other words, can you not accomplish your purposes more directly, and perhaps more quickly, and with less expenditure and less purchase by operating more in the long end than in the short end?

Mr. MARTIN. We had this colloquy the other day and I tried to answer it then by saying that certainly it was questionable if you wanted to reduce the long-term rate more rapidly than it was being reduced, if we might not have done that by direct operations in the long end of the market. I have been able to see that argument and weighed it many times in my mind.

Representative COFFIN. I am not asking it with reference to any particular point of time, although I realize that this is probably essential to the question.

Mr. MARTIN. What I am getting at is, you have the problem of unwinding that operation at a later date. You may want to sell long-

term bonds later to offset them. That is one of the problems, and that is the point I was trying to make about our wanting to be careful that we do not start down a road from which we will find great difficulties in retracing our steps. We may have been overcautious in that. Certainly we ought to consider that very carefully. But my experience has been that it is awfully easy to get started and then find you are caught.

If we accumulated all of our portfolio in the long end of the market and then we wanted to sell securities, we would have nothing but long-term securities to sell.

Representative COFFIN. I agree. The theory of this appeals to me because of the thinness of the long market and the fact that you can get reactions with less movement.

Mr. MARTIN. I think you put your finger right on it. I think what you are dealing with here is a combination of theory and practice. When we came out of a pegged market, we had to go through a difficult adjusting process over a period of several years.

As I said earlier when you were not here, I think the staff memorandum is a first-class job of pointing up the issues that are involved. As a matter of fact, we have discussed virtually all of the issues in there around the open market table.

Representative COFFIN. This is not a fair question, but when you go away from these hearings have you learned anything or is this all duplication?

Mr. MARTIN. I will have learned something; yes. I learn something all the time. Yes; I think definitely I will. However, I don't think there has yet been presented, to my satisfaction at least, a convincing need to change the general techniques that we have been following. I think they ought to be examined, but I have not yet been convinced by what I have heard that they should be changed. That doesn't mean I have not learned anything. I think it is very valuable to have our attention focused constantly on this.

Representative COFFIN. All you can say in answer to this second major question that I asked of you is that it is a matter where the theory has a great deal to commend it?

Mr. MARTIN. I think this is theory, personally. We have differences of opinion in our own group on that. I think the theory has some relevance for me when you are trying to ease interest rates. I have not seen it on the other side. I think that the disadvantages of operating in long-term securities on the other side far outweigh any possible advantages both in theory and practice.

Representative COFFIN. You mean the practice of selling long term?

Mr. MARTIN. That is right.

Representative COFFIN. This leads to a question Mr. Reuss asked you, where he asked you about raising reserve requirements and at the same time going on the market to purchase securities, thus easing money supply.

You said, "Why do that? In essence, are you not operating at cross purposes?" I think that is roughly what you said.

Is this not true? If you raise requirements, and for most banks this works well, particularly if you follow the chairman's suggestion and you raise them very gradually, most banks could adjust to this without a disorderly liquidation of their securities. You might have

banks X and Y that would be placed in a difficult situation. By a judicious purchase of securities and easing of the money market, it is my understanding that this would make it possible for dealers, these 17 important knowledgeable dealers, to sort out banks X and Y and take care of their securities in an orderly way at reasonable prices.

So is not this a limited area but nevertheless one where Mr. Reuss' suggestion is a practical one?

Mr. MARTIN. About sorting it out, I just can't follow it. It doesn't do any good to just offset.

I'm not sure what Mr. Reuss would want to do at the present time. Would we sell long-term bonds and buy short-term bonds? Would we do that? That would just increase the imbalance that we have in our Treasury portfolio that is already unbalanced and—

Representative COFFIN. We are talking not so much about attacking the problem of imbalance; we are talking about raising reserve requirements in a move to combat inflation, but with sort of an anchor to windward, a minor use of purchase of securities to make available money to avoid a disorderly liquidation by some banks that are too tight.

Mr. MARTIN. Apart from that, the fact remains that we are in a given flow. There is a quotation on our building of President Wilson's to the effect that if we had a clean sheet of paper to write on, that would be one thing, but as we don't have a clean sheet of paper to write on, changes can be made only step by step.

It is that process that the Federal has been engaged in since we unpegged the Government securities market; and trying to do what we can to influence monetary policy and make possible the rebuilding of an organized market, regardless of its form and shape, that will be serviceable. That is why your staff's memorandum points up this matter of auction as a technique.

With the Treasury coming to the market periodically—month in and month out, frequently—the problem is entirely different than if you have an entirely different flow of the money supply to deal with and the need of the Treasury to deal with. All of those things have to be weighed.

Mr. Roosa, I think, expressed it very well the other morning. He could not come back today.

Representative COFFIN. I am not asking you to say that as a general policy raising reserve requirements and purchase of securities is the policy that is better than other alternatives. Perhaps I will ask you flatly.

Would you say that at no time under no condition would it be at all practicable to raise reserve requirements and at the same time purchase securities? You believe there is no merit in this whatsoever?

Mr. MARTIN. No, I would not.

Representative COFFIN. That is a candid answer.

Do you know whether or not the opinion of the economists is unanimous on this point?

Mr. MARTIN. No.

Representative COFFIN. If I have time for one final question, we were talking with the insurance people the other day, as Senator Javits indicated, about savings bonds.

As an expert in the money-market, even though this is not under your jurisdiction, I would like to ask your opinion whether there is any merit in exploring the possibility of a bond, either the series E bond itself or a substitute, to be issued by the Government solely to individuals without a termination date and with periodic interest payments determined by the Treasury at rates which will reflect the realities of the market, which would be a variable interest rate with no ceiling and calculated by the Treasury on the basis of criteria that would be articulated, the objective being to increase the 15 percent of the debt that is now held by individuals to a much larger figure. Therefore (a) it would ease the problem of the Government in strengthening the long-term side of the spectrum, and (b) it would stimulate a larger participation by individual citizens.

The question is whether you think this merits exploration.

Mr. MARTIN. With variable interest?

Representative COFFIN. Yes.

Mr. MARTIN. I would not want to make a definite answer on that. I think it merits consideration as all of these suggestions do. I would have to think about that.

Representative COFFIN. That is all, thank you.

The CHAIRMAN. Thank you very much, Mr. Martin.

There are some housekeeping details that I think I should clean up.

First, I was greatly flattered by your complimentary references to the reports which the staff have made and which were furnished you. Did you refer to these five study papers that the staff sent down to you?

Mr. MARTIN. That is right.

The CHAIRMAN. I am very glad to have that in the record. I am very proud of the staff. I think they are doing an excellent and nonpartisan job.

I would also ask unanimous consent that there be printed as a part of the record at the conclusion of the testimony of Secretary Anderson two documents. The first is the material which had been included in the 1956 report of the Governmental Operations Committee of the House, comparing the recommendations of the American Bankers' Association at various times and the action taken by the Treasury at that time. This ran to February 1956. (See p. 1221.)

Without objection, that will be done.

I further ask unanimous consent that the document which we have just received from the American Bankers' Association, giving similar analysis beginning with July 1956, and extending to July 1959, be made a part of the record. (See p. 1225.)

The Chair mentioned in his interrogation of Secretary Anderson that he make informal comparison of a number of cases in which the final decision of the Treasury was either identical with or closely similar to the recommendations of the committee of the American Bankers' Association and those relatively few cases where the final action differed from the recommendations.

I am now going to ask the staff to make a more thorough and more official check of these informal conclusions which I personally make.

I would further ask them to make a study for this later material which I am now putting in the record.

(Information referred to appears at p. 1229.)

The CHAIRMAN. Mr. Martin, you have had a rough week at the hands of Congress and we thank you for your courtesy. Unless the plans of the committee have changed, we are going up to New York next week and hold hearings on the New York money market and dealings with Government securities and quotations of Government securities, the question of margin requirements, auctions, and so forth.

Before you go, Mr. Martin, may I say in this connection I have read your very excellent report in which you oppose an organized exchange market of Government securities. I think I would like to make it clear that this is not what some of us in Congress are proposing. What we are proposing is the auction method on new issues, whereas this analysis treats the subject of organized exchanges on existing issues.

So we hope we may have your advice and help and opinion as we go along to consider the flotation of new issues.

What some of us have been proposing is an auction system for long-time Governments closely analogous to the system which they now use for their short-time issues.

I thank you very much.

(Thereupon, at 12:50 p.m., the committee adjourned, subject to the call of the Chair.)

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