

Representative REUSS. Thank you, Mr. Chairman.

Mr. Weston, you spoke earlier of the differential between present short-term and long-term interest rates. It has been somewhat disturbing to me that short-term interest rates below 4 percent on Treasury bills for example seem to me almost unnecessarily low and particularly in a balance-of-payments deficit situation and long-term interest rates which have hardly come down at all from their peak of last August seem unnecessarily high in terms of what they do to the housing industry, small business, State and local borrowing, and so on.

I think you said that the Federal Reserve System could have done more than it has done to bring longer term interest rates down. Did I hear correctly?

Mr. WESTON. I asserted that the Fed does have the power to affect long-term rates, but this involves some cost, too. The point I am making is that, given some increase in the money supply, the volatile segment of the demand and supply relationships in the money and capital markets are on the demand side and the private sector is not interested in building up 3-month liquidity. They are interested in building up 12- and 18-month and even 3- to 5-year funds, which means that from their own standpoint they are going into the long-term bond markets to build up funds which won't run off and won't be subject to the necessities for repayment during a 5- or 10- or 15-year period of time.

Representative REUSS. I think that the Fed deserves a little criticism for not responding more than it did. You know the Fed back in 1961 or 1962 formally renounced its "bills only" policy or "bills preferably" policy and said, "From now on we are going to buy across the spectrum."

I checked the figures the other day and what happened is that after a few months of adherence to this new policy of rejecting bills only, the Fed went right back to, using Mr. Samuelson's term, "its same old snake oil," and has really been on a "bills only" jag for some time, with a result that its \$3 billion portfolio today is lighter on the long side than it ever was in the heyday of "bills only."

I am wondering in a broader purchasing policy, when they increase the money supply, why not give it across the board instead of just on the short end? I am wondering if such a policy wouldn't have produced a better structure of interest rates today to the help of the housing industry and so on.

Mr. WESTON. In stating that the Fed could reduce long-term rates, I was disagreeing with the proposition that they cannot, but I was not necessarily criticizing the Fed's decision not to. I think these are two separate issues.

Representative REUSS. However, shouldn't they have, and shouldn't they now? They are, in the last few weeks, now buying a few long terms, but shouldn't they really rid their intellectual storeroom of this "bills only" notion?

Mr. WESTON. I make two comments on that.

One, when the Fed operates in the long-term market and produces changes in supply relationships there, and when taken in conjunction with demand relationships produces yield or price effects, the impact—since they are long term—is greater than the presumed impact in the short-term area. This accounts for the tendency to operate in the