

Chairman PROXMIRE. I understand that, but what they have done is not to increase the money supply. They have decreased it in the third quarter and maintained a stable money supply in the fourth quarter and the first quarter of this year.

Mr. TOBIN. I don't think that is what they have chosen to do.

Chairman PROXMIRE. This is what has happened. This is the result of their policy.

Mr. TOBIN. That is what has happened, but the tapering off of credit demands, which is responsible for some of the decline in interest rates, is also responsible for the failure of the money supply to expand.

Chairman PROXMIRE. Yes, indeed, but as Professor Culbertson points out, the tapering off of the demand for money—the credit demand—is because interest rates are the highest they have been in 40 years up until recently and they are still very high on a long-term basis.

Mr. CULBERTSON. Could I make a clarifying comment in reply to his clarifying comment?

Chairman PROXMIRE. Yes. These debates are very enlightening.

Mr. CULBERTSON. I would differ from Professor Tobin in this way. It certainly is true that the change in the economic situation tends to cause a change in the behavior of the money supply, other things equal. My presumption is that if there is a change in the banks' desired reserve positions or a change in the demand for credit, the Federal Reserve offsets that through its provision of reserves. In the absence of such a presumption, it seems to me that our monetary system is fundamentally anomalous. If the economic situation weakens, the money supply goes down. That is a very inappropriate sort of monetary system.

You would be better off going back to gold, since this sort of monetary system is in general terms destabilizing. So my assumption is that the Federal Reserve ought to be offsetting factors affecting the money supply in such a way as to cause it to behave in an economically desirable way. It has the power to do this.

Mr. TOBIN. Of course, it has the power to do so, but that doesn't mean it has been using this power so as to fix any particular statistical aggregate such as the so-called money supply, or that it should do so.

The purpose of monetary policy, in my view, is essentially to try to stabilize, or to make moves in the proper directions, spending for investment, for housing, for inventory accumulation and so on.

Now, spending on these things depends largely on a comparison between the profitability which businessmen, consumers, and others see in acquiring new physical assets and the cost of credit or the yield of alternative uses of their own funds.

There just isn't any simple statistical relationship which tells you what is the proper monetary policy at any moment of time.

Chairman PROXMIRE. Yes, but wouldn't you agree at the present time, in view of the fact that industrial production has not grown in the last month or two, that housing has been in the doldrums for several years, and is only beginning to recover somewhat in the last 2 or 3 months.

As you say so well, unemployment has not moved very much. It didn't decline at all last year to speak of. It has been the same. Automobiles, so many other things that depend to some extent on credit financing have been either stagnating or moving downward.