fensive position against the general tightness of money markets that occurred last year.

Representative REUSS. On the interesting dialog between you two gentlemen a moment ago when Chairman Proxmire was examining, Mr. Tobin, you, I believe, rejected Mr. Culbertson's reaching out toward the money supply as the proper determinant of Federal Reserve monetary policy, and I think I heard you say that the Fed can't really control the money supply. You said, I thought, that it could control bank reserves, but not the money supply.

I would like to examine that, if I am reporting right what you said, with you, because I am not sure I follow you. The Fed, of course, can control the amount of bank reserves by its open-market policy, its reserve-requirement policy, and to a degree by its rediscount policy. That you concede; do you not?

Mr. TOBIN. That is what the Fed, in fact, does. It can control the quantity of bank reserves.

Representative REUSS. Yes.

Mr. TOBIN. It can set the discount rate, and so on.

Representative REUSS. Well now, when a bank gets a reserve, doesn't it almost immediately and inevitably transfer that into an increase in the money supply?

It either lends it to somebody, or it invests it in a security. In either case, unless I need, as I probably do, some educating on this, adding to the money supply.

Just let me finish and then I would like to have you clear this up. It is true, of course, that nonmoney substitutes for time deposits, as you mention, have to be considered, but the Fed can do something about their amount, too.

It, after all, controls reserve requirements on time deposits. Would you lead me out of this thicket?

Mr. TOBIN. Well, I think we have to distinguish between what the Federal Reserve controls absolutely and immediately, which is as you said, the quanitity of reserves and discount rates, and so on, and what they can control more indirectly by moving their immediate and available instruments in response to what they see is happening.

It is true, in a sense, that you can say that the Federal Reserve can control the money supply if they want to, because whenever they see the money supply being different from what they would like it to be, they can push their levers around until they get what they want.

There are other things, too, they could control if they wanted to. They could keep the bill rate at any level they want, if they intervened in the market every time the bill rate diverged from some target level they wanted. But that is quite different from saying that they do, in fact, act that way or that they should, in fact, act that way.

Now as for your point about the tight relationship between the quantity of reserves and the money supply, that is just not true. Although the Federal Reserve supplies a certain quantity of reserves to the banks, and determines the quantity that the banks can have without borrowing, it is the banks which determine how much of those reserves they use, how much they keep as excess reserves, or how much they supplement them by borrowing from the Federal Reserve at the prevailing discount rate.