

other is to ask me to comment on it in the particular terms in which you and Mr. Culbertson choose to define the policy.

Representative REUSS. Take them one at a time.

Mr. TOBIN. I will take them one at a time. Now as for the policy of the Federal Reserve in 1962, as I said earlier, I wish it had been more expansionary. I wish it had. That probably would have meant both a faster rate of expansion of the money supply and lower interest rates at the same time.

And if it had resulted in a 6-percent increase in the money supply, and nothing had happened to interest rates, and to investment and the use of credit and so on, then I wouldn't have been satisfied with what had happened to the money supply.

Actually the reason for the failure of the money supply to expand in 1962 was the Federal Reserve's attachment to a particular target of the bill rate, which they had adopted for international balance-of-payments reasons.

Once they had adopted that target, then the money supply expanded as fast as the banks and the economy wanted more money at a 2½-percent bill rate. They weren't controlling the money supply. They were controlling the bill rate.

If they wanted the money supply to expand faster, they would have had to accept a lower bill rate, to have pushed a lower bill rate, and they didn't want to do that for international reasons.

Now I thought then, and I think now, they were putting too much emphasis on the international reasons relative to the needs of the domestic economy. But this is a matter of whether their policy was appropriate in 1962, not whether some particular figure for the money supply was being achieved in 1962.

Now February 1965 to February 1966: We still had unemployed resources at the beginning of 1965. Subsequently we were having a rapid increase in activity, which accelerated toward the end of the year. The needs for money, therefore, expanded quite rapidly as well. Unemployment was still around 4 percent at the end of that time.

I think it would have been a mistake to take any arithmetical target for the money supply and to say regardless of the extent of the expansion of activity, and that we shouldn't provide deposits in excess of some predetermined notion of what the rate of increase in the money supply should be.

There is in fact no close statistical relationship between money supply and economic activity. If you look at the series for the money supply and for money value of GNP over the last few years, you will find that the velocity of money, the ratio of money to GNP to the quantity of money has not been constant. You would think, to hear these money supply people, that it was a simple thing.

You put in a dollar of money and you get a certain amount of GNP out of it. It is not true. The velocity of money has changed during the past few years. Moreover, it has changed in a predictable direction; namely, it has risen. That is understandable in view of the increase in interest rates which has occurred.

Neither is there any simple, close relationship between the increase in the money supply and the rate of increase in GNP. If you plot one against the other, you get a jumble of noise.

I can't understand why this idea that there is a simple close relationship between expansion of money supply and expansion of GNP has