other reason than because interest rates would fluctuate. It is highly significant that Professor Friedman stands almost alone in contending that income velocity and demands for cash balances are not significantly affected by changes in interest rates. Virtually all other investigators have found very significant effects. They differ somewhat on which interest rates are most influential and how great the responsiveness is, but all find that increases of interest rates reduce velocity. This assures that velocity will behave in a procyclical manner.

Consider, for example, the situation in 1966 when rapidly rising Government expenditures coincided with a strong investment boom. Interest rates would have risen sharply even if the money supply had been increasing at an annual rate of 3 or 4 percent. The rise of interest rates would have induced both business and the public to economize on their money balances, which yield no explicit return, and this would have been reflected in a rise of income velocity. Thus at the peak of interest rates, business and the public would be holding money balances relative to their expenditures which would continue to be satisfactory only so long as interest rates remained at that level. When the boom subsided and interest rates tended to fall, they would demand to hold more money relative to their expenditures, and their attempts to replenish their balances to the new and higher demanded levels would delay and retard the downward adjustment of interest rates and a general easing of money market conditions. Thus what could have been only a mild recession may be translated into a more serious recession or even into a depression, especially if an expansionary fiscal policy is not initiated.

It is for reasons such as these that Professor Friedman's inflexible rule would not yield acceptable results, especially so in view of the fact that he virtually rules out the use of fiscal policies for stabilization purposes. I was pleased to see that the proposal advanced by Congressman Reuss as a basis for discussion avoids these inflexibilities. For one thing, he suggests not just one rate of increase of the money supply but a band of rates between 3 and 5 percent. Then he would allow the Federal Reserve to depart from the band under six specific types of situations. I believe all of these exceptions are essential; perhaps more should be added. I submit, however, that when all the desirable exceptions to the rule are included, we are well on our way toward restoring discretionary power to the Federal Reserve.

I conclude, then, that while it may be feasible to provide more specific guides relating to the objectives of monetary policy, it is not feasible to formulate more specific and appropriate operating guides for the policy actions to be taken to promote those objectives.

I see no workable alternative to discretionary monetary actions. I say this despite the many shortcomings of discretionary policies—difficulties of forecasting, lags in the effects of monetary policies, and so on. The Federal Reserve has made mistakes and will doubtless make more. But one need not think that Federal Reserve officials and their staffs are infallible to believe that their discretionary actions based on flows of current information, on forecasts for the coming months and on continuous revision of those forecasts, will yield better monetary policies than those dictated by some inflexible rule formulated and prescribed months, or even years, in advance.