

Mr. HART. I am trying to work the arithmetic out, but I would think off hand that if we had restricted the growth in demand deposits to 5 percent instead of 6.5 percent, the public would have tried to raise the money in some other fashion, and I suppose this would have brought greater pressure on the whole capital market structure.

Representative RUMSFELD. Your judgment then is that it would not have been preferable?

Mr. HART. I do not think it would have been preferable right at that point, but I guess I am not too happy about seeing these wide swings, either.

I wish there was some way we could reduce the swings, but I am a little troubled as to how you do it.

Representative RUMSFELD. It seems to me that the question recognizes the fact that you are dealing with the lesser of two evils.

Mr. HART. Somebody who wanted demand deposits would have to give them up then, would they not?

Representative RUMSFELD. If the pressure came in the way which you have described.

Mr. HART. Yes. Well, if you have 6.5 percent and you are going to cut it to 5, somebody who wants to hold demand deposits is not going to hold them, because there will be fewer demand deposits.

Now, I assume that if you could not have a demand deposit, you would probably want to hold something else close to it. I think this might have caused quite a bit of pressure in the markets.

Mr. GAINES. Mr. Rumsfeld, I would like to respond to that if I might. It seems to me it is awfully important to distinguish among types of demand deposits. A growth in demand deposits of any given size that does reflect an increase in liquidity in the economy, an increase in the availability of funds that can be spend at the option of the owner of those deposits, is relevant. But in 1967, in my interpretation of what occurred, the largest part of the increase in the money stock, in the demand deposit component of the money stock, represented an increase in compensating balances at the larger commercial banks. This is borne out by the fact of more rapid increase in demand deposits at the larger banks than elsewhere in the economy.

Now, these compensating balances were obtained by the banks because the banks were in the driver's seat last year, after the 1966 credit experience. Banks were able to get the 20 percent or so compensating balances that they had been talking to their customers about for a number of years before that. Compensating balances are not truly spendable funds. They do not increase the liquidity of the holder of the balances in the same way that normal growth in money supply would.

This was a distinctly different type of increase in money stock. If one could sort out or separate out the compensating balance component of last year's growth in money stock to arrive at an estimate of what the true growth in spendable funds was, I think we would find that the growth in money stock last year was well within the 3- to 5-percent band that the committee is concerned with.

Mr. NOYES. Do you want me to have a go at that question, too?

I do not disagree with anything Mr. Gaines has said; but with all of the benefit of hindsight now, we can say that it might have been desirable to deprive some of these corporations of the liquidity that