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Even a discretionary monetary policy needs direction and evaluation

Since actions taken to affect the volume of bank reserves are necessarily and inherently quantitative in nature, it comes rather as a shock to note how imprecise the standards guiding monetary management are at all levels. The lack of guidelines is even more disconcerting since the built-in uncertainty precedent to action makes it impossible to assess or test after the event whether an action taken was of the character, scale, or timing that was intended or should have been expected in the public interest. Little wonder that without standards of direction or evaluation there is a generally uneasy feeling about, or a dissatisfaction with, the performance of monetary management.

It will be useful to divide the possible guidelines for monetary policy into three levels in what might be regarded as a descending order from objectives to policy to execution. First, there are guidelines relating to the ends or objectives to be promoted by the monetary authorities. Next are those relating to the specific monetary actions to be taken to promote these selected ends. And finally there are guidelines for carrying out the actions, that is, open-market purchases or sales, once policy has been determined. The central issue growing out of the present lack of guidelines is not the choice between a broadly discretionary system and a mechanistic system governing policy. It involves rather the level at which discretion is to be exercised—the Congress or its legally constituted agents, the Board of Governors and the Federal Open Market Committee, or an employee of the system commonly known as the manager of “the desk.”

(1) Let us deal first with guidelines relating to the objectives of monetary policy. The Employment Act is quite specific in setting forth major objectives of economic policy: maximum employment, production, and purchasing power. As interpreted by numerous executive department statements and actions, in which the Congress has concurred, these are generally understood to involve maintenance of low rates of unemployment; reasonable stability in the purchasing power of the dollar; a high and stable rate of economic growth; and a stable exchange rate for the dollar. Likewise, the administration and the Congress have interpreted the Employment Act mandate as contemplating a harmonious integration of fiscal and monetary policies. Yet, neither the Federal Reserve System nor monetary policy are mentioned in the Employment Act.

These omissions are difficult to comprehend today, but more understandable when considered in the light of conditions that prevailed at the time of the Employment Act's passage. The country then was fearful that reconversion to a peacetime economy would be accompanied by mass unemployment. Preoccupied with the prospect of a recurrence of unemployment that characterized the thirties, when interest rates