of money; and banking supervision—regulation, inspection, supervision of member banks. Many of its major mistakes have understandably arisen from this schizophrenic character of its functions. This has fostered the confusion of money with credit; of the interest of its members or the banking community in general with the interests of the public at large.

"It has appeared in recent years that the Federal Reserve has increasingly recognized the difference between these functions and has given its monetary role primacy. Unfortunately, the present proposal is in precisely the opposite direction. It subordinates the major function of the system—promoting a stable monetary framework for the Nation—to the minor function—facilitating the operations of a particular set of business firms, its member banks.

"If the Federal Government is to regulate, supervise, and subsidize commercial banks, it had best be done by an agency that is specifically set up for that purpose and has no responsibility for general monetary policy. Far better to separate out these functions than to let them confuse and conceal the operation of general monetary policy. Yet the Federal Reserve proposals go in precisely the opposite direction.

"Aside from these objections on grounds of broad principle to the Federal Reserve proposals, the specific proposals themselves are highly objectionable. In effect, they consist in passing out sizable subsidies on a highly differential basis to particular groups of banks. The Federal Reserve report does not, of course, describe its proposal in this way, but that is precisely what it is.

"A bank that is enabled to borrow from the Federal Reserve receives a subsidy equal to the amount borrowed times the difference between the interest rate at which it could have borrowed these funds elsewhere and the discount rate. At one point the Federal Reserve report cites $2.5 to $3.8 billion as an estimate of the maximum credit extension under *one component of its proposal* (p. 10 for short-term adjustment credit). If the differential between the rate on other sources of funds and the discount rate were two percentage points—a moderate estimate—this item alone could amount to a subsidy at the rate of $50 to $76 million a year!

"And the total proposal surely could involve a subsidy of several times this sum. The subsidy will be paid by the U.S. taxpayers. It is they who provide the funds to pay the interest on the Government securities held by the Federal Reserve which enables it to lend at rates below market rates.

"It may be desirable to subsidize some or all commercial banks—though I am dubious that it is. Maybe, we are now implicitly or explicitly taxing them too highly and should remit the taxes. These are relevant questions. But it seems to me inconsistent with our basic political values that they should be decided by an administrative body like the Federal Reserve rather than by the elected representatives of the people.

"Major issues of principle and policy are involved in the Federal Reserve proposals. It is urgent that they receive full consideration and public discussion.

"Signed, Milton Friedman, professor of economics, University of Chicago.