A meeting of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System in Washington on Tuesday, March 26, 1957, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Hayes, Vice Chairman
Mr. Allen
Mr. Balderston
Mr. Bryan
Mr. Leedy
Mr. Robertson
Mr. Shepardson
Mr. Szymczak
Mr. Williams

Messrs. Irons, Leach, and Mangels, Alternate Members of the Federal Open Market Committee

Messrs. Erickson, Johns, and Powell, Presidents of the Federal Reserve Banks of Boston, St. Louis, and Minneapolis, respectively

Mr. Riefler, Secretary
Mr. Thurston, Assistant Secretary
Mr. Vest, General Counsel
Mr. Hackley, General Counsel-elect
Mr. Solomon, Assistant General Counsel
Mr. Thomas, Economist
Messrs. Bopp, Marget, Mitchell, Roelse, Tow, and Young, Associate Economists
Mr. Rouse, Manager, System Open Market Account
Mr. Carpenter, Secretary, Board of Governors
Mr. Sherman, Assistant Secretary, Board of Governors
Mr. Miller, Chief, Government Finance Section, Division of Research and Statistics, Board of Governors
Mr. Gaines, Manager, Securities Department, Federal Reserve Bank of New York

Mr. Thompson, First Vice President, Federal Reserve Bank of Cleveland

Messrs. Hostetler and Daane, Vice Presidents, Federal Reserve Banks of Cleveland and Richmond, respectively; Messrs. Parsons

and Coldwell, Directors of Research, Federal Reserve Banks of Minneapolis and Dallas, respectively; Mr. Willis, Financial Economist, Federal Reserve Bank of Boston; and Mr. Kester, Economist, Federal Reserve Bank of St. Louis.

Chairman Martin noted that Mr. Fulton, alternate member of the Committee from Cleveland, was unable to attend the meeting today because of illness but that Mr. Thompson, First Vice President of the Cleveland Bank, was in Washington. The Chairman stated that while he did not think it desirable to open up the meetings of the Committee as a regular procedure, he felt it important that a Reserve Bank be represented by one of its executive officers whenever possible. He suggested, therefore, that Mr. Thompson be invited to attend this meeting in Mr. Fulton's absence, although he emphasized that this should not be considered a precedent for inviting persons not regularly associated with the Committee to attend meetings in the future.

There being no objection to Chairman Martin's suggestion, Mr. Thompson entered the room at this point.

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the Federal Open Market Committee held on March 5, 1957, were approved.

Before this meeting there had been distributed to the members of the Committee a report prepared at the Federal Reserve Bank of New York covering open market operations during the period March 5 through March 20, 1957, as well as a supplementary report covering commitments

executed March 21 through March 25, 1957. Copies of both reports have been placed in the files of the Committee.

Mr. Rouse stated in response to Chairman Martin's invitation for comments that projections of reserves prepared by the New York Bank and by the Board's staff for the two weeks ending March 27 and April 3 were close together, but the projections were quite far apart for the week ending April 10. However, he observed that the differences would probably disappear as the April 10 week approached. Mr. Rouse went on to say that if any member of the Committee had suggestions for improvement in the reports of open market operations he would be happy to receive them.

Mr. Robertson said that he would like to make a few comments on the operations that had been carried out since the March 5 meeting of the Committee and that he wished to make it clear that these comments were being made as dispassionately as possible. He then made a statement substantially as follows:

At the last meeting of this Committee, there was a great deal of discussion as to need for, and the manner of, conducting open market operations so as to aid Treasury financing during this month. A variety of views were expressed. It was evidently agreed that the general aim of policy at this time should be to maintain about the same degree of restraint on expansion that had prevailed; at the same time it was recognized that System operations should take into consideration temporary pressures on the market resulting from Treasury financing operations.

Differences of opinion related largely to the timing and degree of System aid to the market. Some felt that anticipation of needs, thereby giving assurance that reserves would be available, was essential to assure a successful Treasury financing operation. Others felt that System aid to the market should not be given until need

was evident. The Chairman's summary was that the majority was not in favor of giving undue encouragement to Treasury financing and he expressed recognition of the difficult problem presented for the Account Management.

Review of System operations since that meeting indicates that they were conducted with considerable emphasis upon the forthcoming Treasury offering, and market developments suggests a pronounced response to these policies. In the week ending March 13 System purchases were moderate and net borrowed reserves increased to over $400 million, yet the behavior of the money market, while firm, showed no signs of acute tightness. At the end of that statement week the midmonth float increase, together with a reduction in Treasury balances at the Reserve Banks, was expected to supply a substantial volume of reserves. Nevertheless the Account Management continued to purchase securities through Wednesday, March 13.

Again on Monday, March 18, notwithstanding the easy reserve position for that statement week and the absence of any particular pressure on the market, the Management again entered the market and made outright purchases of bills for both cash and regular delivery. This particular operation was designed to aid Treasury financing and also to anticipate reserve pressures that would develop the next two days, although projected weekly averages indicated a relatively easy position. Purchases at that time were inconsistent with the customary policy of refraining from operating in the market the day of a Treasury bill auction. Also on that day subscriptions were being received on the new Treasury offerings. These purchases were promptly followed by a pronounced strengthening of the market for Government securities. Before the end of the week the bill rate in the market declined below the discount rate.

There were many factors other than System operations bringing about this change in the market. Some of these were difficult to predict, but some were evident and question may be raised whether the System needed to contribute as much as it did to easier money, particularly in view of the general aim of current policy. If the Committee continues its policy of restraint on credit expansion and if credit demands should continue strong, it is questionable whether this level of yields and prices of Government securities will be maintained.

The reason for bringing this record to the attention of the Committee is to raise questions for the Committee and the Account Management to consider for guidance in

> conducting operations in the future. In the first place, this experience indicates the risk of endeavoring to anticipate market needs rather than waiting for them to develop before taking action. The major question is whether System operations during a period of Treasury financing should guide the market or merely endeavor to maintain an even keel. Another question is whether operations should be such as to result in a lowering (or raising) of market rates relative to those prevailing at the time of the Treasury announcement and those likely to prevail under current System policy after the financing is completed. Shouldn't we scrupulously try to avoid misleading either the Treasury or the market as to the level of rates at which a new issue may be floated and be maintained in the near future? Measures to ease the market prior to or during periods of Treasury financing run this risk. This experience also raises another question as to technique of operations in general, namely: is too much effort directed toward evening out day-to-day changes in reserve positions, and particularly projections of such changes, which sometimes turn out to be unnecessary? Shouldn't the weekly averages be the more decisive data?

Chairman Martin suggested that Mr. Robertson's statement be furnished to the members of the Committee so that they could study it carefully. He then called upon Mr. Rouse for comments that he might care to make at this point.

Mr. Rouse stated that he felt the reports of open market operations that had been furnished to the Committee covered fully what the account had done during the past three weeks and why the operations had been carried out as they had. He felt that the Account Management had taken a very substantial risk in allowing reserves to stay as tight as they had during this period. Some fortunate breaks had permitted the situation to work out satisfactorily, including a distribution of reserves that avoided serious strain in the central money market, even though there were pressures in the market that were not apparent from

the figures presented. Mr. Rouse went on to say that he understood that the Committee recognized a secondary responsibility in connection with financing operations of the Treasury, to the extent that additional pressures on bank reserves and the money market that might interfere with these operations should be avoided. Some members of the Committee might not realize the serious situation that the Treasury faced in this particular financing operation. When the terms were first announced, there was a good deal of doubt in some quarters as to whether the offering would prove acceptable and the situation had been "touch and go" for several days.

Mr. Hayes noted that Mr. Robertson had spoken of weekly average figures as being important in determining account operations. He called attention to the fact that during the three weeks ending March 20, negative free reserves averaged approximately $300 million and that they were as high as $425 million during the week ending March 13. At the meeting on March 5, there had been some discussion of negative free reserves around $200 million or in the $0-200 million range, and he did not recall any suggestions for negative free reserves higher than $300 million during this period. From a statistical standpoint, Mr. Hayes felt that the operations had kept fairly well in line with what the Committee contemplated. During the week of March 13, when negative free reserves rose to $425 million, the account had refrained from purchasing bills in the volume that would have been necessary to achieve the reserve figures discussed by the Committee because it

thought it foresaw additional reserves from float during the following week. Mr. Hayes pointed out the difficulty of carrying out the open market operation, adding that at many stages during the past three-week period the New York Bank was consciously trying to maintain as much restraint as possible in the market while still giving recognition to the fact that the Committee had some responsibility for the Treasury financing. Mr. Hayes said he did not believe there was much, if any, anticipatory buying of securities such as Mr. Robertson had implied.

Mr. Robertson stated that he was unable to see any justification for some of the activities that had been carried on by the Account Management. He had the impression that operations had not been based on figures or feel of the market but rather on what the account felt was going to happen the next day or later, and primarily with the idea of making the Treasury financing a success without regard to what the Committee had authorized as shown by the minutes of the March 5 meeting.

Chairman Martin said that he would like to point up this discussion. He thought it was clear that Mr. Rouse felt he was operating within the authority given by the Committee at the March 5 meeting.

Mr. Rouse stated that this was, of course, correct. His only fear was that the operations had been keeping the situation too tight in terms of the Treasury's financing: in the week when negative free reserves averaged $425 million he thought there was a risk of giving the impression that the System was going to a little tighter policy than the Committee had contemplated.

Mr. Robertson said that this was not a criticism of Mr. Rouse but of all of the members of the Committee: there was a tendency to try to justify what had happened. At the March 5 meeting, he said, the consensus seemed to be that a majority of the voting members of the Committee favored not easing the situation but maintaining as tight a position as had existed prior to that meeting. Primary emphasis was not placed on any figures.

Mr. Hayes raised the question of what had indicated such great ease during this period. The bill rate had gone down, he agreed, but a special and unusual demand for bills had driven that rate down, just as in the summer of 1956. Mr. Hayes felt that this had no real connection with the general state of the market; in this period, the bill rate was not a true measure of over-all tightness and its decline did not indicate a basically easier money market situation.

Mr. Robertson said that he was certain that both Mr. Rouse and Mr. Hayes felt that the System account's actions were within the intent of the Committee. What he was casting reflections on, he said, was the inadequacy of the steps the Committee had taken to specify what it wanted. Personally, he felt that the actions taken in this period were not in accord with the actions desired by the Committee.

Mr. Johns inquired whether there had been any Treasury request to anyone in Washington or elsewhere for assistance in connection with the recent financing.

Chairman Martin stated that he would not say that there had been a request for assistance, and Mr. Rouse also said that there had been no request made to the New York Bank. Chairman Martin went on to say that he and Mr. Rouse had attended a luncheon with Treasury officials at which the latter were told of the Committee's policy that would apply during this period. He felt that the Treasury had been given a clear impression that it would have to carry on its operations within the limits of the Committee's policy, and Mr. Rouse stated that the statements could not have been more blunt.

The Chairman went on to say that he felt it a good thing that Mr. Robertson had raised the questions he had regarding the operations of the System account. He felt that anyone who had such questions should not hesitate to bring them up--in fact, there was a duty to raise them. In this particular case, the Chairman remarked that an item had appeared in the press in which credit was given to the Chairman of the Committee for the success of the Treasury's financing because of comments he had made in an address to the National Press Club on March 15.

Mr. Shepardson inquired as to the relationship between Mr. Rouse's comment that the success of the Treasury's financing had been "touch and go" and the fact that the offering had been heavily oversubscribed.

Mr. Rouse stated that the Treasury had made a judgment that the banking community would be willing to buy a substantial amount of

the securities. It had received advice that, instead of reopening the 3-3/8 per cent note, it should offer a 3-1/2 per cent one-year security with a convertible feature. The Treasury chose to disregard that advice and it ran a risk based on its judgment that the banks would enter subscriptions. This judgment turned out to be correct.

Chairman Martin said that as a matter of information, it was the judgment of some of the Committee staff as well as that of the Chairman of the Committee that the rate offered by the Treasury would not be sufficient to make the issue a success. This judgment turned out to be wrong. The Chairman also stated that Mr. Shepardson's inquiry could be answered by the statement that the money market was more ready for the securities than many people believed to be the case.

Mr. Allen stated that he had been on vacation during the period of the Treasury financing but that his impression was the same as that of Mr. Robertson, that is, that the account had operated in a way that seemed to denote an inappropriate degree of responsibility to the Treasury.

Chairman Martin said that this view could easily be read into the record and that this was why he asked the Manager of the Account to express himself. He felt it was clear in Mr. Rouse's mind that he was not operating with responsibility to the Treasury but on the basis of what he conceived to be the operating instruction of the Federal Open Market Committee.

Mr. Shepardson recalled that there had been frequent discussions of the level of reserves as a guide to operations. The bill rate had also been referred to, and that rate had now declined after having been at a somewhat higher level. He inquired as to the significance of the bill rate as an indicator of a decrease in restraint during the past few weeks.

Mr. Rouse stated that in these circumstances he did not feel that the decline in the bill rate indicated a lessening of the degree of restraint. He suggested that the rate on Federal funds had been an indicator of restraint during this period, and the effective rate for such funds had remained at 3 per cent throughout the period. A higher bill rate might to some extent be a reflection of general pressure in the banking system, particularly when banks held bills and needed to sell them. By and large, however, Mr. Rouse felt that during the period under discussion the decline in the bill rate had reflected principally the Treasury's decision not to continue adding to each weekly issue, just as the higher bill rates in February and early March had reflected principally the additions to the weekly issues being made at that time.

Mr. Hayes stated that he agreed that the reduction of $200 million in the March 11 auction by the Treasury of the weekly bill offerings had had an effect on the rate through decreasing the supply of bills available. Chairman Martin added the comment that he thought this probably had more to do with the decline in the bill rate during this period than any other factor.

Mr. Robertson said that he would disagree with the statement that the bill rate was not to any extent an indicator of tightness or easing, to which Mr. Rouse responded that while the bill rate was a factor it was not the prime index of pressure in the money market.

Upon motion duly made and seconded, and by unanimous vote, the open market transactions during the period March 5 through March 25, 1957, were approved, ratified, and confirmed.

Chairman Martin next called upon Mr. Young for a statement on the economic situation.

Mr. Young stated that the staff memorandum distributed under date of March 22, 1957, presented a current review of economic and financial developments in the United States and abroad and that he had prepared for presentation at this meeting an analysis of the basic economic problem now confronting the System. He then read a statement as follows:

The staff report on current economic tendencies pictures a sidewise movement of activity over all at inflated price levels. This morning, instead of enumerating highlight developments included in the report, I should like to direct my remarks to what seems to me the basic economic problem now confronting System policy. That problem relates to the conflict that can and does arise for monetary policy at certain points between the short-term business adjustment objective and the long-term stabilization objective. Such a conflict presents itself sharply at this particular juncture.

In its post-accord official literature, the System has made much of adapting flexibly and promptly to changing credit market and business conditions--seasonal and cyclical; leaning against the wind, it is called. On the other hand, the System's literature has also strongly affirmed a longer-run goal of a stable value for the dollar, recognizing that this stability can only be relative, not absolute. How then should monetary policy react when it is presented with

evidence of slackened momentum of cyclical advance after some 30 months of sustained rising activity, and after a depreciation in the purchasing power of the wholesale dollar over these months of about 6 per cent and of the consumer dollar of over 3 per cent?

As students of economic cycles have many times observed, each cyclical swing is a unique unit of experience. Certainly, the present one has been. It got first stimulus from consumer outlays for houses and durables, purchased heavily on credit. This development was in direct response to the exceptionally easy credit conditions prevailing just after ebb tide of the last cycle. The massiveness with which this stimulus took hold necessarily induced, after a period, a massive acceleration effect in the form of business plant and equipment expenditures. There were, of course, other circumstances (such as already high wage costs and much technologically obsolescent plant and equipment) favorable to this result. But had these circumstances not been present, accelerated capital investment would still have been sizable.

An unusually big capital investment response to the consumer outlay stimulus had several implications. It meant that total demands for credit would indeed be heavy. It further meant that savings would need to increase substantially if monetary expansion were not to get out of control. Then, it meant that interest rates of necessity would have to rise to a higher level. Finally, since additions to the resource supply would need to be largely diverted to producing goods for the future, thus generating additional income without enlarging short-run supplies of end products for current use, rapidly rising business investment meant that commodity and service markets would be under heavy demand pressure, likely to result in some advance in prices.

The broad dimensions of the central economic problem then unfolding were recognized by the Open Market Committee in its discussions over the early spring of last year. Accordingly, a policy course was set, directed to resisting inflationary pressures as they intensified. Such temporary relaxations of resistance as were made, to meet transient shifts in the economic climate, actually seemed to work as stimuli to inflationary trends.

Although relative stability of price levels had generally prevailed for over three years following the post-Korean transition to flexible monetary action, a considerable amount of discussion had gone on in economic and business circles as to whether a little inflation, say 2 or 3 per cent per annum, might not be a good thing, perhaps an essential thing to assure

that private capitalism would provide the sustained high employment levels which the community was asking of it. With this discussion as background, business saw monetary policy, in combating the 1953-54 recession, undertake a massive enlargement of the credit base. Shortly thereafter, business confronted a strong and rapid expansion in aggregate demand. Advances in price quotations, business found, were in fact supported by market demands; wage-cost concessions to labor could be readily passed along in market prices. Industries that had modernized or expanded earlier realized handsome profits; those that had lagged behind moved swiftly to catch up.

Creeping inflation was no longer a theory, it was a fact being realized. Moreover, the process was predicted to continue, with more and more confidence, for the longer-run. Had not monetary policy validated the immediate postwar price level? Had not the post-Korean price level also been substantially validated? Had not monetary action aggressively met the threat of serious recession in 1953-54? Even a research subcommittee of the CED on the issues of longer-run creeping inflation could not reach enough agreement that price stability was a desirable social end to prepare a policy statement on the subject. Little by little, the business community convinced itself that creeping inflation was an attribute of the new era.

Those businesses that borrowed to finance investment during the first two years of this cyclical upswing, experienced with advancing prices, either a very low interest cost or a negative interest carry. Little wonder, with prices continuing to advance and expectations of a longer-run uptrend increasingly widespread, that business demands for short- and long-term credit multiplied. The real interest cost to consumer borrowers over this period also worked out to be in their favor.

Let me digress a moment to explain this idea of a negative interest carry in consequence of inflation. Any illustration must suffer from oversimplification.

Assume that a year ago, a manufacturing company borrowed $1,000,000 from an insurance company for one year at 4 per cent interest. The proceeds of the loan were to help finance capital expansion in process. The capital expenditures then made would at today's prices cost $1,080,000. The company saved $80,000 by the timing of its investment, while incurring a $40,000 interest expense. In real terms, it enjoyed a negative interest carry of $40,000, and even more than this after tax benefits of the indebtedness. In addition, the company was able to maintain or increase its share of the market as

compared with competitors who did not expand at that time. Furthermore, by applying to its well-timed investment the more liberal depreciation provisions available since 1954, the company strengthened its internal cash flow. It thus improved its capacity to return again to the credit market at some future time.

The point of these observations is that one tool of monetary action to restrict demand for credit--the cost of money--has been seriously blunted over the past year and a half by depreciation of the dollar. This development has come before a significant rise in savings has occurred. that is, before the investment-savings gap has been effectively closed. Indeed, depreciation of the dollar has wiped out a part of the higher interest returns essential to establishing a better balance between credit demand and savings supply.

Given loss of momentum to business advance and the appearance of uncertainties regarding future market trends, monetary policy is now getting under pressure to demonstrate again its flexibility by prompt adaptation to relaxed output, employment, and credit market tensions. If credit ease is permitted to develop, or is actively fostered on grounds of uncertainties, before more competitive conditions emerge in those markets experiencing the greatest expansion of demand, then the only conclusion for the business and consumer community to reach is that the dollar depreciation of the past year and a half is to be validated. In the light of the widely-held view that, to sustain high employment, creeping inflation is desirable, and in any case inevitable, such a conclusion would invite also the expectation that further inflation is highly probable.

Spread of this expectation would rapidly activate new spending and borrowing, further increasing the turnover of deposit money. Instead of a period of rolling adjustment in output and prices under more actively competitive conditions and in preparation for a new stage of advance without inflation, immediate resumption of inflationary tendencies would threaten. In recent reports to this Committee, we have several times stressed the basic strength of demand factors in housing and automobile markets as well as the still strong incentives for business investment, even without inflation.

These remarks, of course, have a moral. The Committee needs to consider carefully at this time whether it should not regard the objective of a stable value for the dollar as overriding the objective of adjusting flexibly and promptly to short-run cyclical changes in activity. It needs to weigh the

risk that monetary policy may lose strategic opportunity to make its discipline effective, keeping in mind that, as experience of the late 1920's shows, such opportunity can be lost--and lost forever.

From mid-1955 through 1956, capacity in major materials and power output lines was utilized intensively, as it was also in producers' equipment and construction areas. With the huge additions to industrial capacity of the past two years and with a larger manpower supply, we may at last have attained a situation in which competitive forces, with rolling adjustments, can themselves do much of the work of stabilizing the purchasing power of the dollar. As long as savings are being translated promptly into spending through the intermediation of the credit market, there will be a financial environment favorable to the interplay of competitive forces toward this end--if these forces are given a chance to play.

At the request of several members of the Committee, it was understood that a copy of Mr. Young's statement would be distributed following this meeting and that, as usual, his remarks would be included in the minutes of the meeting.

Mr. Thomas then presented the following statement on recent credit and financial developments.

Credit developments during the past three or four weeks show the anomalous combination of continued large demands for credit with some decline in money rates and a firming of bond yields. To some degree these conflicting developments may be attributed to System operations to provide reserves during the difficult period of large tax payments and the receipt of subscriptions for a $3 billion Treasury offering.

Some elements in the market have apparently interpreted System operations as indicating a shift of policy toward less restraint. Views as to likely development of slacks in the economy both support this interpretation and re-enforce its market effect. The acquisition and holding of a substantial amount of Treasury bills in Chicago and the willingness of Chicago banks to build up substantial borrowings at the Reserve Banks is one influence toward a decline in bill yields. The decline in yields reflects also the effect of the reduction in the amount of weekly bill offerings and reinvestment

of the proceeds of maturing Treasury issues being redeemed for cash on March 22. The eventual offsetting effects of making payment for the new offerings, which are more remote and will be felt more gradually, are apparently not being anticipated. Whether the current easing of money rates is more than transitory will presumably be determined by the course of credit demands after these temporary influences have spent themselves.

New security issues continued in large volume during March, with corporate issues, at about $1-1/4 billion, exceeding $1 billion for the fifth consecutive month--the highest sustained level on record. Compared with other recent periods, a larger proportion of financing is being effected through public offering and less through private placements, and also there are more stocks and convertible bond issues. New securities offered by State and local governments were somewhat less in March, following two months of heavy volume. Dealers' unsold stocks of these issues, which increased sharply in February, have remained relatively large. The stock market has continued at a low level of trading activity with prices close to the lowest point of the past year.

The Treasury has been a net supplier of funds to the market, despite the fact that this is a period of heavy tax receipts. While Treasury borrowing has been larger than usual, its balances have been reduced to exceptionally low levels. Much of the borrowing, moreover, has come from the banking system at a time when demands on banks are seasonally lighter than usual. After March 22, however, Treasury balances will increase again to more normal levels and the new borrowing should build up substantial pressure on the banks beginning March 28. In the first half of April, the Treasury will have very large outpayments, thus returning funds to the market. From mid-April until early June cash receipts and payments are expected to be approximately in balance. Large outpayments in the first half of June will reduce the Treasury cash balance to around a minimum, but net receipts in the last half will rebuild it. Additional financing of a substantial amount will be needed in July. Early financing through additions to the weekly bill issues and through an exchange for maturing F and G bonds will not only reduce July borrowings but avoid a possible squeeze in June.

Bank loans, after the wide swings in December and January, showed no striking development in February. During the first three weeks of March, according to preliminary figures, loans increased sharply. Although the increase did not reach the

high record of last year, it was much larger than in the corresponding period of other years. Commercial loans in the three weeks increased by over $1.2 billion, compared with $1.4 billion in the same period last year. Loans on securities showed a much smaller increase than last year, and the increase in all other loans was also somewhat smaller this year. Loans on real estate have declined in recent weeks.

Demand deposits at banks have continued to show little more than usual seasonal changes. In other words, seasonally adjusted deposits show little or no growth. Time deposits at commercial banks, however, continued to increase at what may be considered as a fairly rapid pace. The increase at weekly reporting banks since the end of November has exceeded $1-1/4 billion, compared with no change in the same period a year ago. No doubt, this growth and the leveling out of demand deposits, reflects some shifting of balances from demand to time accounts, as well as perhaps some shifting from other forms of savings to commercial banks, attracted by the higher interest rates. This trend makes it difficult to interpret the significance of changes--or the lack of change--in demand deposits. Turnover of demand deposits has continued to increase, maintaining an annual rate of growth of about 7 per cent.

Required reserves in the past four weeks have conformed fairly closely to the usual seasonal pattern increasing by nearly $400 million in the first three weeks of March and probably decreasing by over $100 million this week, on a weekly average basis. The continuing low level of the Treasury balance at the Reserve Banks maintained at times only by transferring $100 million from the Stabilization Fund Account, has made more reserves available than might have been expected while float appears to have absorbed on balance more than usual. System purchases of securities, including repurchase agreements, supplied over $330 million of reserves in the first three weeks of March, but sales will absorb over $100 million this week. Net borrowed reserves increased from a weekly average of a little over $200 million in the last week of February (revised downward by about $100 million from the first reported estimate) to over $400 million in the second week of March. The average declined to about $150 million in the statement week ending March 20 and is estimated at around $250 million for the current statement week.

Looking into the near future, reserve requirements next week will be affected by important offsetting factors--the usual April 1 decline in deposits in Chicago and the increase in Treasury tax and loan accounts resulting from payment for the new issue. On

balance a moderate increase in required reserves is to be expected. In addition reserves will be absorbed by the restoration of the Treasury balance at the Reserve Banks to a normal level and by the usual end-of-month decline in float. Net borrowed reserves might average as much as $800 million in that week in the absence of System action to supply reserves. They will continue rather large in the week ending April 10, although a sharp decline in Treasury tax and loan accounts should bring about some reduction in the volume of required reserves. Thus, rather substantial System purchases--$400 or $500 million might be needed in the next statement week to prevent unduly severe tightening in the money market.

Reserve demands in subsequent weeks will depend to a considerable extent upon how the money market makes use of the large volume of funds to be paid out by the Treasury in the first half of April, as well as upon the course of bank credit. Payments by the Treasury will draw funds from tax and loan accounts at banks, thus draining reserves from some banks, but at the same time funds will move into other accounts. If private demand deposits show only usual seasonal changes, required reserves will tend to decline. Net borrowed reserves should, therefore, also show a declining tendency.

On this basis, any System operations to supply reserves in the next week or two of tightness should be followed by sales to absorb reserves. If credit demands do not exceed the usual seasonal pattern and some restraint is still needed, sales should be as much as half of the preceding purchases. If credit demands should not come up to the amounts projected, then less restraint would be in order and borrowings should be permitted to decline. But if there should be a greater than seasonal credit expansion (such as is indicated in the New York Reserve Bank's projections of required reserves in the next three months), the additional reserve demands should be met through additions to member bank borrowings and not through open market operations. To follow a course of providing reserves necessary to keep down borrowings under these conditions would be in effect feeding inflation through the Treasury--a result contrary to the policy directive.

Under those conditions policy should not be directed toward maintaining either a definite volume of net borrowed reserves or a definite level of bill rates. Interest rates should be permitted to rise. Rates and borrowings should be permitted to reflect the forces of credit demands playing upon a normal supply of bank credit. Policy should be determined on the basis of the behavior of the economy in general--the level of production and

employment and the pressure on prices. Although there are some indications of a leveling off in these economic measures, current credit demands are still large, and as long as all available funds are being borrowed and put to use, a serious decline in economic activities cannot be said to be in process.

Chairman Martin called upon Mr. Hayes at this point for an expression of his views regarding the economic situation and the policy to be pursued by the Committee.

Mr. Hayes' statement was as follows:

1. While the view is now rather widely accepted that the boom has lost much of its buoyancy, it is impossible to tell at this juncture whether the economy is heading for a decline or whether the present sideways movement can be relied on to continue for some months, with perhaps a renewed upward movement in the making. On the whole, recent data have been reassuring.

2. Consumer demand, industrial production, and employment remain at or near record levels, but they are no longer rising appreciably. In fact, production has been showing a tendency to decline slightly, probably to a large extent because of a decline in inventory accumulation. There is evidence that some manufacturers are reducing raw material inventories, while finished goods inventories are being increased moderately at the retail level, especially in the automobile industry.

3. Steel production continues to recede and may pull the March index of total industrial production below the February level of 146. However, there is some likelihood that the decline in steel largely reflects inventory adjustments and may not carry far below the 90 per cent level during the second quarter.

4. The most conspicuous "soft spot" in the economy is the residential construction outlook. In February residential starts fell to a rate of 910,000 units, the lowest figure since early 1949. While several types of remedial measures are under discussion, there is no clear prospect of a pick-up. However, other kinds of construction remain so strong that no great slack is apparent yet in employment of building labor.

5. The recently-released SEC-Commerce survey of actual and anticipated plant expenditures confirms that this major upward force in the economy is leveling out. It is now estimated that

such expenditures will be only 6-1/2 per cent ahead of 1956 as compared with a 22 per cent gain in 1956 over the preceding year.

6. Some weeks ago we spoke of the disparity between declining scrap and raw material prices and rising finished goods prices. Since the end of January the general index of wholesale prices has shown little change, while consumer prices have risen further.

7. Developments in the field of bank credit have tended to confirm the other signs of reduced upward pressure in the economy. Thus total loans of reporting member banks rose during the four weeks through March 13 by less than two-thirds as much as a year ago, and about the same ratio applies to the change in total loans of the New York banks in the two weeks ending March 20, in which period borrowing for tax purposes played a leading role. The final outcome of the tax period, however, is still uncertain; the increase in business loans at New York banks in the last two weeks was one-fifth less than last year, but the increase at Chicago banks was greater than a year ago.

8. Underwriting by banks was the major factor responsible for the success of the Treasury's recent cash offering. Thus while a difficult problem has been successfully met, it is clearly incumbent on us to provide sufficient reserves to enable the banks to take up their subscriptions on March 28 without creating undue money market strains.

9. Other credit and capital markets appear to be about in balance. In the stock market, trading continues rather lethargic.

10. Turning to credit policy, we feel that the elements of stability in the present business situation are sufficiently impressive to justify our maintaining a general policy of credit restraint pending further appraisal of the probable direction of the next major change in economic activity. At the same time, we should recognize that economic developments themselves--and a growing recognition that the boom is less buoyant than it was--have meant some relaxation of strained conditions in the credit markets, even though the level of net borrowed reserves has generally been close to that of last autumn. This tendency toward less intense restraint has been enhanced by the distribution of reserves as between the central money market and the rest of the country. Perhaps the phrase "passive restraint," reportedly used by the Chairman in a recent speech, correctly conveys the spirit of our activities in recent weeks.

11. We can see every reason to prevent the degree of restraint from becoming more intense than it has been in

recent weeks. Reserve projections suggest that if we are to maintain net borrowed reserves of say, $200 to $300 million, it will be necessary to make open market purchases of some $500 million in the next week or so, largely to enable the banks to take up their subscriptions to the new Treasury issues. Purchases of this order, applied to a relatively limited market for Treasury bills, and coming at a time when corporations are adding to their bill holdings for June tax purposes, will probably drive bill rates even lower and will make the bill rate itself a poor criterion of credit policy for this period. We might add that redistribution of the securities acquired by the banks on March 28 should tend to prevent any material decline in short-term rates generally, and the passage of the April 1 tax date in Chicago should release considerable amounts of bills thereafter. Under these circumstances, we would lean toward use of a target of $200 to $300 million net borrowed reserves and would not be disturbed to see a temporary substantial drop in bill rates. We would, however, permit net borrowed reserves to rise above the suggested target level if this seemed necessary to prevent an unduly easy "feel" in the money market.

12. We would not favor any action at this time which would suggest a major change in credit policy, and any change in the discount rate therefore would appear undesirable. The directive as presently worded seems to cover adequately the credit policy which we have proposed.

Mr. Johns said that three weeks ago he had expressed the view that a policy of restraint should be continued, perhaps indicating a target of net borrowed reserves of $200 million with a preference for being on the easier side of that figure rather than on the tighter side. If there had been a change in his attitude in the last three weeks it would reflect less apprehension about the development of a downturn in the economy. Therefore, he would now continue a policy of restraint. While he would rather not make errors, he would prefer that such errors as were made be on the side of restraint at this time. He was discouraged about the use of net borrowed reserves as a guide and hesitated

to mention any figure at all. He could see no need for changing the discount rate now. In sum, he would maintain a firm condition for the time being.

Mr. Bryan expressed appreciation to Messrs. Robertson and Young for the very carefully prepared papers they had presented. Mr. Young had made a number of points that he hoped would be subject to comment by the Committee when the members had had an opportunity to study the text of the paper.

With respect to short-run credit policy, Mr. Bryan said that a factor that he believed to be pertinent was the trend of long-term interest rates and the demand for savings in relation to the supply. This might affect what the Committee would like to do in the short run. He suggested that we may be in for a generation of an upward trend in interest rates.

As for the economic situation, the Sixth District was continuing essentially in a boom situation, Mr. Bryan said, with most figures performing somewhat better than those for the nation as a whole. There are almost no excess reserves in the district, and borrowings both in the Federal funds market and at the Reserve Bank are high. On the national picture, his comments would be about like those of Mr. Johns. Mr. Bryan said that he had quite consistently felt it was too early to adopt an easing policy, and if there had been any change in his views recently it would be that the economy had shifted toward greater ebullience and

confidence. As a consequence, he did not feel that any easing action whether through open market intervention or the discount rate was called for at this time. As a matter of fact, without criticizing anyone, he felt that since the turn of the year the Committee had again been following a policy of "inadvertent ease." The situation was much easier than the Committee's judgment indicated at the beginning of the year, when he understood that policy was to attain a degree of restraint approaching that of late November and early December of 1956. The interest rate structure had been permitted to ease more than had been desirable in the light of all the circumstances, Mr. Bryan said, and this unfortunately had created in the minds of practically all businessmen and bankers the impression that we were on the verge of a major policy action looking toward further easing. The policy of inadvertent ease had contravened the intentions of the Committee, Mr. Bryan felt, and he would prefer that the Committee get into a posture of greater restraint. He did not think a target of free reserves particularly useful. He would not make purchases in the market with the bill rate under the discount rate; rather, he would intervene in the market by making sales of securities with the bill rate below the discount rate. He also commented that reactions to changes in the bill rate confused him; when the rate rose to 3.25-3.30, there tended to be a feeling that things were too tight; but when the bill rate went below the discount rate, it ceased to be a good measure of economic restraint.

Mr. Williams said that activity in the Third District continued to mark time with no clear sign of moving either up or down.

Department store sales turned up sharply in the week ending March 16 after substantial declines in the two preceding weeks. For the past four weeks, sales were 6 per cent below a year ago, and they were down 2 per cent for the year to date. Television sales in Philadelphia were off about 50 per cent and new automobiles were moving slowly, with registrations during the first two months of the year about 15 per cent under a year ago. During the first half of March registrations in Philadelphia were down 31 per cent. Claims for unemployment benefits had been slightly above those for the preceding year in February, but during the past three weeks such claims had been below those filed last year. Sentiment on the business outlook had not changed significantly in the past few weeks, Mr. Williams said. The consensus seemed to be that 1957 would be a good year, characterized by both strong and weak spots, with total business activity expanding at a slower rate than last year.

Turning to credit, Mr. Williams said that the volume of business borrowing in the Third District during the past four weeks was slightly higher than a year earlier. Tax borrowing had been about the same but business loans had turned up in mid-February and had risen more in this four-week period than in 1956. After presenting data covering recent changes in business loans at several large Philadelphia banks, each of which showed an increase since mid-February, Mr. Williams concluded his remarks by stating that as he viewed the situation business and financial developments did not now indicate a change in the discount rate or in the

directive for open market operations. Personally, he agreed with Mr. Young that the System should allow rolling readjustments to continue.

Mr. Thompson said that the trend of business in the Cleveland District appeared to be much the same as in the United States as a whole. It was fulfilling the more optimistic forecasts made at the turn of the year, remaining fairly stable close to top records. There were some weaknesses and different degrees of weakness. Steel had been in somewhat of a down trend. The automobile industry was one of the weak spots with sales failing to show the expected upward surge. Inventories of new automobiles were high, and it was expected that the automobile industry would have to cut back production goals. Foundries were bearing out this expectation, with producers of castings for automobiles quite unhappy about the orders they have been receiving, while foundries making heavy castings were doing well. The machine tool industry had a six-month order-backlog and although that was lower than in the past, the situation was considered to be good with employment high. With respect to appliances, one major producer had scheduled on the basis of a reduction in over-all demand and was watching inventories carefully; another producer was basing production on an increased demand. Residential builders were unhappy, Mr. Thompson said, but nonresidential work in process continued at a very high level.

With regard to credit, Mr. Thompson reported that business loans of reporting member banks in the Fourth District had increased more in March of this year than last, somewhat to the surprise of bankers who

as recently as two weeks ago had expected demand to be lower than last year. Banks do not seem to feel as tight as they did, and borrowings at the Reserve Bank have been less than a year ago.

Mr. Thompson said that while there was some surface appearance of stability in commodity prices, the basic pressures appeared to be upward although there had been some weakness among industrial prices. A further advance in steel prices was anticipated. Wage rate increases this year would put pressure on costs and this might be reflected in commodity prices. All in all, Mr. Thompson felt that there should be no letup in the restraint exerted through open market operations and there should be no change in the directive of the Committee that would indicate a softening of attitude.

Mr. Shepardson said that he was particularly pleased with the statements that Messrs. Young and Thomas had given the Committee this morning. It seemed to him that the Committee was constantly being influenced--perhaps subconsciously--by the bias toward inflation and by the fear that the Committee's operations might be at a point of turning the economy down. He recalled that he had expressed views upon a number of occasions that the Committee may not have been sufficiently tight in its operations--not as tight as it had intended. At the preceding meeting he had expressed the hope that during the Treasury financing this month the Committee would not get into a position where it would have to turn around and increase pressures again. There had been discussion of maintaining the same degree of restraint, but Mr.

Shepardson wondered whether what had happened was not a result of the fear that the Committee might make conditions too tight. He likened the situation to that of a person who was a little nervous and disturbed while driving a team of horses and who, without letting go of the reins, permitted them to slip through his hands. Personally, Mr. Shepardson said, he would prefer that the Committee "take another bite" rather than permit the reins to slip further. He would not suggest any specific figure of reserves or any level of bill rates. In the past he had thought both of these had some useful significance as guides, although this was a matter for the technicians. He would hope that the Committee would get a firmer grip on the reins so that it would have restraint that would combat the growing feeling among many persons that a certain amount of inflation must be accepted. Mr. Shepardson did not think the Committee should accept inflation as inevitable, and it should take every step that it could to curb such a development.

Mr. Robertson said that he concurred completely in Mr. Shepardson's comments. As to the economic situation and prospects on which monetary policy should be based, he would adopt the comments Mr. Young had made. One way of doing what Mr. Shepardson suggested was to let the discount window have a bigger share in providing the reserves needed, rather than to try to do the whole job through open market operations. It was obvious that we must engage in open market

operations, Mr. Robertson said, but he hoped that they would be minimized and that some of the slack would be taken up through the discount window. He certainly would do nothing to ease, he would "take another bite" as Mr. Shepardson had indicated, and he would be sure that any errors were on the side of tightness.

Mr. Leach said that business activity in the Fifth District continued mixed with little net change. The coal industry was on the strong side, with production increasing slightly in recent weeks in response to satisfactory domestic demand and a strong export market. Cigarette output was high and orders at shipyards were exceedingly large. The textile industry on the other hand had continued to exhibit weaknesses in production, orders, prices, and profits. Operations at furniture factories dropped slightly during February and were also slightly under the February 1956 levels. The lumber situation appeared somewhat weaker, with production off and stocks up sharply. Income received by farmers from cotton and tobacco this year would probably be down from 1956 as a result of large acreage reductions.

Mr. Leach said that since the last meeting of the Committee he had given considerable thought to bank loans in the district and had talked with a number of senior officers of large banks about their loan demand. The sharp seasonal rise in business loans during the latter part of 1956 led to repayments after the turn of the year that were considerably larger than a year ago. A bottom was reached in

outstandings in early February and since then there have been increases in business loans, closely comparable to those of 1956. In the Fifth District gains in these loans had been slightly greater than in the corresponding period of 1956, while in the United States they had been somewhat smaller, possibly due to a lower level of tax borrowing.

As to the strength of current loan demand, Mr. Leach said that about two-thirds of the bankers with whom he talked stated that underlying demand for business loans was as strong as ever. Others felt that demand continued very strong but not quite as feverish as it was last year. The demand for business loans did not furnish evidence that the economy was weakening.

On balance, Mr. Leach said that he did not look for a significant change in business activity in the near future either in the Fifth District or in the country as a whole. Any movement in either direction was likely to be slight. As to policy, he thought the Committee should continue to maintain the present degree of pressure, resolving doubts on the side of restraint. Any lessening of restraint would, in his judgment, quickly result in an undesired expansion of loans. Consistent with this view, he did not think the discount rate should be changed at this time.

Mr. Leedy said that the most important thing that had taken place in the Tenth District recently had been the snow storms that

had brought considerable moisture throughout the drought-stricken parts of the district. This did not mean the drought was ended, but the moisture furnished had been important and would have a favorable effect on the outlook.

Mr. Leedy said this was not the time to tighten up. We all recognize the soft spots and the general leveling off in the economy. He felt that, without actually applying additional restraint, the Committee might give a little more evidence of an intent to keep bank reserves under pressure than it had been able to give in the recent past. This had been a difficult period, Mr. Leedy said, with the convergence of corporate tax payments and Treasury financing. For the period immediately ahead, he felt the Committee should indicate that its purpose was not to relax but that it had a policy of continuing at least the degree of restraint that had been intended in the recent past.

As to business loans in the Tenth District, Mr. Leedy said that there had been a very large increase in recent weeks. He felt that as a guide the Committee might watch more closely what was developing in business loans. He thought that a level of $200-300 million of net borrowed reserves might prove too low to obtain the desired restraint, and he referred to the negative free reserves of over $400 million in the second week of March as not having an unwanted effect. The Committee should lean toward tightness rather than to the contrary. Mr. Leedy said he would go along with Mr.

Robertson's view that the additional reserves the banks apparently were going to need should be supplied to a greater degree through borrowings than through open market operations. No change in discount rate or the wording of the directive was needed at this time, Mr. Leedy said.

Mr. Allen said that in the Seventh District there was evidence that the leveling in general business activity was a little more pronounced than in the country as a whole. Employment in Michigan and Indiana, for instance, was less than a year ago because the gains in nonmanufacturing were not sufficient to offset the declines in manufacturing employment. In Illinois, Iowa, and Wisconsin, the declines in manufacturing employment had been more than offset by gains in nonmanufacturing employment.

Department store sales in the Seventh District were running slightly lower than a year ago, Mr. Allen said, but there is a belief that when the late Easter has arrived, sales for the year to date will have passed the figures of last year. With respect to the automobile situation, Mr. Allen said that sentiment in Detroit during the past few days had been less optimistic, or more pessimistic, than in recent weeks.

In summary, Mr. Allen felt that the level of general business activity was still high. The so-called "bubble" seemed to be off the boom, which was to be desired. Mr. Allen said he supposed the Committee's task was to do what it properly could to see that the high level of

business activity continued without any bubble. He continued to feel that for the present monetary policy should mark time, that is, it should not add to or subtract substantially from reserves, and it should confine actions to the temporary requirements of an orderly market situation.

Mr. Allen concluded his remarks by saying that he liked and agreed with the comments Mr. Hayes and others had made to the effect that guides to operations not be exclusively net borrowed reserves or feel of the market, but a combination of both.

Mr. Powell said that business activity in the Ninth District during the first quarter of 1957 appeared to have held its own, with some measures of activity up and others down. On the soft side there was persistent weakness in residential construction, some easing in inventory accumulation, a slight increase in unemployment, a decline in prices of some basic raw materials such as copper, steel scrap, and aluminum, and more or less business pessimism generated in part by recent downward trends in stock market prices and profit margins. On the strong side the district economy showed a high level of non-residential construction, rising employment, a high level of incomes, a favorable outlook for farm machinery sales, farm prices holding at a slightly higher level than a year ago, iron ore mining scheduled for a strong opening this spring, and a strong demand for commercial and industrial loans.

Both city and country member banks suffered a greater deposit loss thus far this year than last and while liquidation of loans and

investments had aided banks in meeting the large deposit outflow, there had been a rising level of borrowings from the Federal Reserve Bank and through the Federal funds market.

In recent weeks melting snow had improved the soil moisture supply and opened up more ranges for livestock grazing. Breeding cattle and ewes had come through the winter in seasonally good condition. Although soil moisture had been improving, it was still inadequate in the Dakotas and Montana and generous rains would be needed this spring to start crops off satisfactorily. Farmers' intentions to plant indicate a substantial reduction in wheat acreage partly because of the heavy sign-up in the soil bank program.

Mr. Powell stated that he, too, had been much interested in Mr. Young's comments. He felt that it would be helpful if Mr. Young could also comment on steps that might be taken to offset the rising turnover of bank deposits. He concluded his remarks by saying that the Committee should continue firm restraint in every way it could, although he would not favor an increase in the discount rate.

Mr. Mangels commented that the earthquake damage in the Pacific Coast area over the past weekend was not of major proportions.

As to general business, the Twelfth District was continuing a fairly strong tendency although there were indications that in the next few months the rate of increase would not be as great as over the past year. Nonagricultural employment in February was 5 per cent higher than a year earlier but level with January of this year. There had

been a slight increase in claims for unemployment insurance in February largely because of weather conditions. Plywood mills in the Pacific Northwest were operating at about 75 per cent of capacity. Department store sales were off in February and March but this might reflect the late Easter this year. On the other hand, new automobile registrations seemed to have shown a little spurt in recent weeks with quite an increase having been reported in California during February. January and February together would show a total about the same as a year earlier. Residential and nonresidential construction were down, but there was a fairly large backlog of nonresidential construction and a good program of building was expected for the year.

Mr. Mangels said that bank loans in the Twelfth District for the four weeks ending March 13 moved contrary to the national picture by showing a moderate decrease. He reported that a survey of individual banks in connection with corporate tax borrowing indicated relatively little demand for such loans as compared with last year. There was still some pressure for term loans although banks were trying to get out of that field. Several banks indicated that loan demand was brisk, but the majority indicated less demand than in the past. Savings deposits were increasing and it was reported that at one bank in California such deposits were growing at the rate of $1 million a day.

Mr. Mangels expressed the view that there might be developing a better balance between supply of and demand for goods than has

existed in the past. Certainly in the Twelfth District an easier situation was developing. Despite this, he would not modify the Committee's policy of restraint although he felt that the Committee should not take undue action to increase pressure. He had in mind a net borrowed reserve figure in the $200-300 million range as suitable for a policy guide during the coming period. He would make no change in discount rates at this time.

Mr. Irons said that confidence in the Dallas District was stronger than it had been several weeks earlier, largely reflecting the widespread rains and plentiful moisture supplies during recent weeks. Heavy rains for the district generally had improved subsoil moisture as well as surface moisture. He noted a word of caution among cattlemen in Houston, who urged that cattle ranchers not rush to restock their herds. However, the rains had had a very marked effect on confidence of businessmen generally. One aspect of this was the fact that some farmers now appeared to be unhappy that they participated in the soil bank program even though soil bank payments might range from $100 to $125 per acre on some irrigated cotton land.

Mr. Irons went on to review the industrial situation in the Dallas District. He stated that both residential and nonresidential construction had been higher recently than a year ago. Department store sales had been somewhat lower after adjustment for the late Easter, but an increase was anticipated. The automobile business had turned better the past month, with registration of new cars in Dallas

and Houston in the first half of March 24 per cent higher than a year ago and 17 per cent above February. Sales conditions were extremely competitive, however, with terms about what buyers of cars want.

Borrowings at the Federal Reserve Bank continued negligible, Mr. Irons said, and business loans recently were off. Bankers say that loan demand continues strong but point out that their position is much easier than six to nine months ago. As to credit policy, Mr. Irons felt that in view of the national situation, the Committee should make every effort to maintain a degree of firm restraint on banks. He felt that the Committee had lost ground since last November, stating that there had been an unconscious tendency when in doubt to be on the side of ease. Policy should be flexible, Mr. Irons said, and the Committee should "lean against the breeze," but should guard against being motivated to action at the first "flutter of the leaves." Errors should be on the side of restraint, and he hoped that some substantial part of the funds that would be needed during the next few weeks would be supplied through the discount window. At the moment, he would not change the discount rate although he felt such a change might come.

Mr. Erickson said that he too felt Mr. Young's statement was excellent. In the First District, business continued its sidewise movement. Most figures were not now as high as they were a few months ago but were higher than a year ago. There had not been the expansion

in commercial and industrial loans that had been reported elsewhere either for tax purposes or for other reasons. On the other hand, since the preceding meeting there had been greater use of the discount window. Last year a peak use of the discount window was reached in May, and recent borrowing had been almost as high as last May. Mr. Erickson said he would suggest no change in the discount rate or in the Committee directive. As to open market operations, he would resolve any questions on the side of restraint. He still hesitated to set any figure of net borrowed reserves as a target, but he hoped that as far as possible credit needs would be supplied through the discount window.

Mr. Szymczak recalled that two meetings ago he felt relatively that the Committee should try for a figure of $200-400 million of negative free reserves. At the March 5 meeting, he felt it should relatively strive for a figure of $0-200 million of negative free reserves because of the conditions brought about by the Treasury financing and corporate tax borrowing. At the present time, he felt the Committee should strive for a degree of restraint indicated by a figure of $200-300 million of negative free reserves. Nothing now indicated a change in the economy sufficient to call for a change in credit policy at this time. It appeared that activity would continue at a high level and the Committee was more likely to need to absorb reserves, than supply them. Mr. Szymczak said that he would recommend getting back to the degree of restraint that the Committee contemplated a few weeks ago.

Mr. Balderston said that there had been so many sound things said so well that he hesitated to add any comments. He noted Mr. Bryan's suggestion that the Committee bear in mind both the long run objectives and the immediate problem. Mr. Balderston said he was concerned about the long run because it seemed to him that certain factors created the framework within which the Committee and the System must operate. He referred (1) to the continuing inadequacy of savings to meet investment demand, (2) to the increased Governmental spending at both Federal and local levels, (3) to the lessening adequacy of fiscal policy as a partner in restraint, and (4) to the numerous Governmental proposals to use short-term credit for long-term purposes. Mr. Balderston said that at least one or two of these factors seemed to have changed for the worse. He referred not only to the very disturbing suggestion that Government make direct loans but to the policy of having the Federal National Mortgage Association make long-term mortgages with short-term money.

As to the future, Mr. Balderston said that rolling adjustment seemed to him to be the thing the Committee should aim for. It should be watching the time when rolling adjustments ceased to roll. A measure would be when aggregate demand ceased to be as strong. Applying this test to the present, Mr. Balderston said that it seemed to him that country-wide demand for bank credit was still almost as strong. The apparent ease with which new capital issues had been floated was in part explained by redemptions of F and G Treasury bonds. Thus,

the Treasury had supplied some of the funds that had made it easy for corporations to get their capital requirements taken care of.

During the next three weeks, Mr. Balderston said he personally would like to see the Committee supply considerably less credit through the open market than either forecast indicated. One of the forecasts indicated net borrowed reserves of $630 million and the other of $800 million. Instead of operating as the Committee normally would, Mr. Balderston suggested supplying considerably less credit than these forecasts indicated, thereby forcing member banks to use the discount window. Mr. Balderston emphasized that he was on the side of restraint.

Chairman Martin said that he, too, had been impressed with Mr. Young's paper.

The Chairman stated that he would align himself with what seemed to be the consensus of the meeting, that errors in System account operations be on the side of restraint rather than of ease. He felt this particularly because of the fact that the Treasury would have to come to grips with the problem of long-term money, and the System should do nothing that would mislead the Treasury on what that rate should be. He took it that the consensus today was that the Committee should maintain the directive at its present form. The only figures of net borrowed reserves mentioned had been in the $200-300 million range with one suggestion of $400 million, the Chairman noted. He assumed that both feel of the market and behavior of the market would be recognized in carrying on operations for the System account and that the Manager would endeavor to make his errors on the side of tightness rather than of ease.

Mr. Rouse said that he agreed with the Chairman's comments but that he would like to go one step further in order to avoid any misunderstanding. His approach to operations during the next three-week period, during which a considerable volume of reserves must be supplied, would be to let the market come to the System. He would not contemplate going out to seek Treasury bills. This might mean some backing up in the rate and would require purchases only in order to avoid getting an extreme situation on the tight side.

Mr. Hayes said that he would like to comment on the peculiar nature of the problem from a day-to-day operating standpoint and of the criteria that should be used in carrying on operations. It was very difficult to say what the criteria should be. Looking ahead, it seemed clear that in the immediate period the System should let the banks depend on borrowing to obtain a good part of needed reserves. He illustrated the difficulty of using statistics as guides by noting the suggestion made at earlier meetings this year that the Committee should restore the degree of restraint that existed last November. Mr. Hayes pointed out that at that time net borrowed reserves averaged less than $200 million whereas during the last few weeks they had averaged around $300 million, despite which there was a greater spirit of ease recently than last November. At this meeting it had been suggested that net borrowed reserves might be in the $200-300 million range but Mr. Hayes stated that this would not do the job of restoring the restraint that existed last November. To do that might require

net borrowed reserves of $400, $500, or $600 million. Mr. Hayes stated that he wished to emphasize the danger that existed in any instruction that might be given to the System account on the basis of statistics. He had been impressed with Mr. Thomas' suggestion regarding the use of week-to-week developments in bank credit as a guide for Committee policy.

Mr. Robertson stated that he realized the difficulty of using any figures. References to figures for an earlier period were made in relation to the feel of the market at that time. This was a relative matter, and Mr. Robertson said that he did not think the Committee could rely on a specific figure as the sole indicator of the degree of tightness at a given time.

Mr. Shepardson said he wished to emphasize the same point that Mr. Robertson had mentioned. The Committee should not get confused by the references to figures since, as Mr. Hayes had pointed out, one figure might create a certain degree of restraint at one time but it would not cause the same degree of restraint at another time. He gathered that the Chairman's statement of the consensus was intended to indicate that in the immediate future needed reserves might come largely through the discount window and not through open market operations.

Chairman Martin said that Mr. Rouse as Manager of the System Account was trying to point out the difficulty of bringing this about: until the banks came to the System, we could not supply reserves through the discount window. The liquidation of long-term Treasury

debt and its conversion into short-term debt had been a constant drag on the System's operations.

Mr. Rouse noted that at the present time member bank borrowings were at a level which in other periods would cause a great deal of concern, because they would cause strain in the market. However, on analysis, with Chicago banks borrowing $400 million out of a total of $900 million, these figures caused concern to no one.

Chairman Martin said he wished to make it clear that anyone was privileged to speak again as to how he felt operations for the System account should be carried on.

Mr. Allen said that he hoped that at some time there would be an opportunity for discussion of Mr. Young's phrase that monetary policy had "validated price levels."

Chairman Martin said that he felt it would be desirable for all members of the Committee to study the paper that Mr. Young had prepared and to have a discussion of its content at a later meeting.

After Mr. Rouse had stated that he had no recommentations for change in the Committee's directive, the Chairman suggested that it be renewed without change, and there was no disagreement with this suggestion.

Thereupon, upon motion duly made and seconded, the Committee voted unanimously to direct the Federal Reserve Bank of New York until otherwise directed by the Committee:

(1) To make such purchases, sales, or exchanges (including replacement of maturing securities, and allowing maturities to run off without replacement) for the System open market account in the open market or, in the case of maturing securities, by direct exchange with the Treasury, as may be necessary in the light of current and prospective economic conditions and the general credit situation of the country, with a view (a) to relating the supply of funds in the market to the needs of commerce and business, (b) to restraining inflationary developments in the interest of sustainable economic growth while recognizing uncertainties in the business outlook, the financial markets, and the international situation, and (c) to the practical administration of the account; provided that the aggregate amount of securities held in the System account (including commitments for the purchase or sale of securities for the account) at the close of this date, other than special short-term certificates of indebtedness purchased from time to time for the temporary accommodation of the Treasury, shall not be increased or decreased by more than $1 billion;

(2) To purchase direct from the Treasury for the account of the Federal Reserve Bank of New York (with discretion, in cases where it seems desirable, to issue participations to one or more Federal Reserve Banks) such amounts of special short-term certificates of indebtedness as may be necessary from time to time for the temporary accommodation of the Treasury; provided that the total amount of such certificates held at any one time by the Federal Reserve Banks shall not exceed in the aggregate $500 million;

(3) To sell direct to the Treasury from the System account for gold certificates such amounts of Treasury securities maturing within one year as may be necessary from time to time for the accommodation of the Treasury; provided that the total amount of such securities so sold shall not exceed in the aggregate $500 million face amount, and such sales shall be made as nearly as may be practicable at the prices currently quoted in the open market.

Chairman Martin noted that a copy of a report by the Subcommittee on Emergency Planning (Messrs. Shepardson, Hayes, and Robertson, Chairman) had been distributed under date of March 26, 1957, and at his request Mr. Robertson commented briefly on the content of the report and the recommendations contained therein. He stated that a staff group had reviewed

the emergency planning program and activities of the Federal Open Market Committee and that it was their unanimous opinion (1) that the structure of the planning was sound and required little change, and (2) that the effectiveness of the emergency planning activities from here forward would depend essentially on training provided by simulated problems posed in successive Alerts.

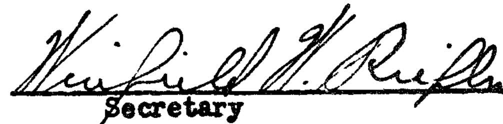
The report recommended, Mr. Robertson said, that a process of review similar to the one embodied in the current report be undertaken annually to see that all phases of the emergency program were kept current with developments in the general emergency planning of the Government. One of the specific recommendations was that the training of System personnel at the Securities Trading Desk of the New York Bank be continued and that personnel from the Board's staff be included in the participating group. It was also recommended that more personnel in Federal Reserve Banks be cleared so that they could participate effectively in all parts of the emergency planning, that at least two individuals from Federal Reserve Banks be sent to the Board to participate as full members of the Board's organization during each major Alert, and that each Federal Reserve Bank again review its organization to see that a sufficient number of its staff had been trained to participate effectively in these emergency operations. Mr. Robertson went on to say that in the event the Federal Open Market Committee approved the report, the Subcommittee on Emergency Operations would undertake to see that the recommendations

were carried out.

After discussion, the report of the Subcommittee was approved by unanimous vote.

It was agreed that the next meeting of the Federal Open Market Committee would be held at 10:00 a.m. on Tuesday, April 16, 1957.

Thereupon the meeting adjourned.



Secretary