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, May 3, 1960, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Balderston
Mr. Bopp
Mr. Bryan
Mr. Fulton
Mr. King
Mr. Leedy
Mr. Robertson
Mr. Shepardson
Mr. Szymczak
Mr. Treiber, Alternate for Mr. Hayes

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

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

Mr. Young, Secretary
Mr. Sherman, Assistant Secretary
Mr. Kenyon, Assistant Secretary
Mr. Hackley, General Counsel
Mr. Thomas, Economist
Messrs. Brandt, Eastburn, Marget, Noyes, Roosa, and Tow, Associate Economists
Mr. Rouse, Manager, System Open Market Account

Mr. Molony, Assistant to the Board of Governors
Mr. Koch, Adviser, Division of Research and Statistics, Board of Governors
Mr. Keir, Chief, Government Finance Section, Division of Research and Statistics, Board of Governors
Mr. Knipe, Consultant to the Chairman, Board of Governors

Messrs. Hickman, Mitchell, Jones, Daane, Rice, and Einzig, Vice Presidents of the Federal Reserve Banks of Cleveland, Chicago, St. Louis, Minneapolis, Dallas, and San Francisco, respectively

Mr. MacDonald, Assistant Vice President,
Federal Reserve Bank of Richmond
Mr. Willis, Economic Adviser, Federal Reserve
Bank of Boston
Mr. Holmes, Manager, Securities Department,
Federal Reserve Bank of New York

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meetings of the Federal Open Market Committee held on March 22 and April 12, 1960, were approved.

Before this meeting there had been distributed to the members of the Committee a report of open market operations covering the period April 12 through April 27, 1960, and a supplementary report covering the period of April 28 through May 2, 1960. Copies of both reports have been placed in the files of the Committee.

With further reference to developments since the Committee meeting on April 12, 1960, Mr. Rouse made the following comments:

I should like to start off with a comment on the change in the bank reserve situation since the time the Committee last met. On April 27, at the close of the last statement week, required reserves were $551 million higher than they were on April 11 and, at the same time, member banks were able to support this with $250 million less borrowing from the Reserve Banks. The figures involved in these calculations are tricky and I shall not attempt to detail them. However, I feel satisfied, on both an average and a day-to-day basis, that, as suggested be done during the discussion at the last meeting, natural factors provided the bulk of the reserves that enabled the banks to meet the higher required reserves at the same time that they were reducing their borrowing from the System. This is brought out most clearly in the comparison of April 11 and April 27 figures, as on an average basis the picture is somewhat obscured by the special repurchase agreements to aid the dealers on Good Friday.

The action taken by the Committee to assure Government securities dealers of System support over the Good Friday week end was of considerable help in restoring a better atmosphere in the auction of the special April Treasury bills three weeks

ago. And, while there was an element of good fortune involved, in that market factors supplied fewer reserves than anticipated over the week end, this assistance to the Treasury did not involve any undue ease in the money market. Although, without System assistance, the results of the auction could have been far worse as far as the Treasury was concerned, it is no secret that the Treasury has been far from happy with its experience in auctioning one-year bills, and the decline of the rate on April 15 bills from the 4.60 per cent established in the auction, with a stopout of 4.74, to close to the 4 per cent level in a short time did nothing to reassure them on this score.

While on the subject of the one-year bills, I might mention that the memorandum circulated to the Committee prior to this meeting comments in detail on the swaps undertaken by the Account to acquire $10 million of the July 15 bills. Since this was our first operation under the authorization given by the Committee and since the subject is to be reviewed later on in this meeting, we felt that such a detailed description might be helpful. In the future, however, if the authorization is extended, we would prefer to report further acquisitions of one-year bills on swaps on a more routine basis. While they would be fully covered in the regular written reports to the Committee, we would not normally expect to report them in such detail.

Treasury bill rates moved somewhat lower during the interval between Committee meetings, but there was very little change in prices of Government notes and bonds, reflecting the Treasury refunding of $6.4 billion securities maturing May 15 which is currently under way. The Treasury's offering in this refunding of a one-year certificate at 4-3/8 per cent and a five-year note at 4-5/8 per cent has been well received by the market. Rights were quoted at a premium at the market close last night, and the when-issued certificates and notes were both quoted at par and 2/32 bid to par and 3/32 asked. The Treasury decision to grant rights to holders of the maturing issues was undertaken reluctantly, and only after Treasury representatives had canvassed the market on April 22. It is my own feeling that the Treasury might have been able to refinance on a cash basis without excessive difficulties, although there are always unforeseen problems when an innovation is attempted. Moreover, it would have been desirable for the Treasury to have had a larger cash balance as protection against such contingencies. I might add that one factor involved in the relatively generous pricing of the new issues being offered was the Treasury's desire to avoid large-scale attrition and to have the new issues stand up well in the secondary market. Advisers to the Treasury suggested that attrition might be large. There also was

some feeling in Treasury circles that pricing would have to take into consideration the probability of some improvement in the business outlook. I believe they had the pending release of the McGraw-Hill survey particularly in mind.

Thereupon, upon motion duly made and seconded, and by unanimous vote, the open market transactions during the period April 12 through May 2, 1960, were approved, ratified, and confirmed.

Supplementing the staff memorandum distributed under date of April 29, 1960, Mr. Noyes made the following statement with regard to economic developments:

The abrupt transition from winter to spring that took place in a large part of the United States in April brought with it impressive improvement in several current economic indicators. Most impressive, perhaps, was the spectacular rise in sales at department stores, which probably carried them to a seasonally adjusted level close to the record 150 index of last July. Auto sales also improved substantially in the first 20 days, and scattered reports suggest that in the last 10 days they continued in good volume. The fact that the Board's index of industrial production will probably hold even, or decline only one point, in the face of further cutbacks in steel during April will be regarded by many as an encouraging sign.

The McGraw-Hill survey released on Friday, but widely circulated in advance, provided less tangible, but equally welcome, evidence of underlying strength. Claims for unemployment compensation declined a little in April, up to the week ending April 23, but on the other hand they remained at a relatively high level--a fifth more than a year ago. In fact, the employment situation generally continued to be a major cause of concern in many areas, as employment, especially of blue-collar workers, continued to lag behind expectations.

At the same time, first-quarter profits were generally regarded as disappointing, and in the last few days the stock market has slipped back to its March low--about one-eighth below the January high.

Most of the other information that has recently become available relates back to March or the first quarter. We know now that diffusion indices based on leading indicators showed sharp declines in March and that some dropped to levels that have heretofore heralded major downturns. However, their poor

showing in one month, strongly influenced by comparison with the peak of poststrike activity, is not too meaningful.

The early estimates of gross national product for the first quarter, released by the Council of Economic Advisers, are already subject to revision as more data for March become available. Inventory data now suggest that the rate of inventory accumulation was even larger than the $9 billion estimate--perhaps nearer to $10 or $10.5 billion, thus narrowing the small gap between the GNP estimates and the $500 billion generally forecast. At the same time, this additional inventory component in the first-quarter data diminishes the chances that the second-quarter total will compare favorably. Should inventory accumulation drop back to a low figure, it is hard to pinpoint expansive factors that would provide $7 or $8 billion of additional expenditure, at annual rates, to replace it in this quarter, since a month of curtailed activity in many lines, especially steel and autos, has already gone by. Hence, even if final takings expand somewhat in the current period, we may well find ourselves with a GNP at midyear that does not show substantial improvement over the first quarter. Furthermore, the prospects for substantial improvement in the employment picture are not too good. Present rates of unemployment have persisted despite much smaller additions to the labor force than demographic factors indicated. Thus, we may see more than the usual seasonal increase in those seeking employment this summer, and unemployment rates may push upward in the absence of considerable strengthening in the demand for workers.

It is too early yet to expect any reflection of the somewhat improved availability of mortgage funds in residential building, and the decline in new construction put in place in April was largely a reflection of the lower levels of starts in February and March. However, the rise in residential vacancies in the first quarter to a new postwar high was widely noted, and may temper considerably the pace of any upward shift in residential building, even if mortgage money continues to ease.

Most of the bearish information relates back to the earlier part of the year, and quite a bit of improvement may show up in the April data that become available in the next few weeks. With the coming of spring, some sense of euphoria seems to spread across the country, but there is little or no real exuberance. The situation is certainly not one that could be characterized as a burgeoning economy, straining at the leash of limited credit availability, and the prospect of developments that could be so characterized, in the near-term future, seems very slight.

Mr. Thomas presented the following statement with regard to the financial situation:

Available information indicates that economic activity is showing a fairly satisfactory pickup from the first-quarter lull, but without exuberance. This is evident in the financial area. In some respects financial developments since the last meeting of this Committee represent a reversal of trends then in process. Interest rates, which were then rising following a sharp decline since January, have again turned down. Total loans and investments of city banks increased more than usually in April, after showing a declining tendency for some time. The increase, moreover, reflected substantial additions to bank holdings of Government securities and loans on securities, while business loans declined somewhat--contrary to previous trends. Deposits at banks--both demand and time--also increased. As a result, previous indications of an upturn in the money supply seem to be confirmed.

These shifts reflected greater bank and less nonbank participation in the Treasury financing during April than in other recent operations. City banks acquired a major portion of the new two-year notes, a substantial amount of the one-year bills, and some of the long bonds. They also made a large volume of loans to dealers in Government securities, which in turn substantially increased their positions. The large bank and dealer acquisitions, together with the marked upturn in bank deposits, indicate that the prolonged increase in nonbank holdings of Government securities may have halted or slackened--at least temporarily. This means that recent Treasury issues, underwritten by banks and dealers, yet need to be distributed to other investors.

Federal Reserve operations played an important role in facilitating the flotation of the Treasury issues. Substantial purchases of bills in the market and liberal repurchase accommodations to dealers have provided additions to the reserve supply. In contrast to recent trends, required reserves increased much more in April than had been projected on the basis of the estimated increase in Treasury deposits at banks and the usual trends in other deposits. In addition, Easter currency demands absorbed more reserves than had been expected, but in the past week much of this has returned. Continuation of float at a higher level supplied some reserves. Member banks thus were able to meet the substantial increase in required reserves and at the same time reduce somewhat further their borrowings at the Reserve Banks.

Discount rates on Treasury bills in the past three weeks have fluctuated somewhat at below the levels reached on April 12,

at the time of the auction of one-year bills, but above the low points to which they dropped in late March and early April. Yields on Treasury bonds, after rising in the first two weeks of April, have steadied. Yields on seasoned corporate bonds have remained comparatively steady, but those on State and local government securities have risen some in the past week. Although new issues have been in moderate volume, some of them have moved rather slowly into hands of investors and in some cases offering prices have had to be reduced. Indications are for a continued moderate volume of new issues in May.

Exuberance in the stock market, which appeared in late March and early April, was brief, and stock prices are back close to the lows of the year. Liquidation of stock market credit seems to continue slowly.

With respect to current and future Federal Reserve operations, it can hardly be said that the System is following a particularly restrictive policy. Although the discount rate remains at 4 per cent, reserves have been made available and member bank borrowings have declined to a moderate level with a lessening in the number of borrowing banks. Rates on Treasury bills--except for the new one-year issue--have remained below the discount rate. Question may be raised as to how much, if any, credit restraint is likely to be needed in the near future.

Although economic activity is at a relatively high level and will probably continue its expanding trend, the expansion is likely to be moderate and the threat of a boom in this country does not seem to have much basis, although boom conditions exist in some other countries. There are many structural elements in the current economic situation of this country that may serve to prevent or limit any revival of speculative tendencies, without the need for credit restraint. Some of them are familiar, some have been pointed out in the reports presented to the Committee, others are perhaps less obvious.

The elimination of the Federal Government deficit has removed one of the most important factors working toward inflationary tendencies, but there can be speculative or other unsustainable developments without a deficit. Evidences of excess capacity and of some elements of slack in the economy, however, may help to dampen any such tendencies. Growth in the labor force has not kept pace with the population of working age, yet reported unemployment continues larger than at some previous times of high activity. The margin is not large, but there are growing signs of successful efforts to economize on the use of labor. The high level of wages and other labor costs encourages such attempts. This tendency is likely to continue.

There is also an increased margin of unused productive capacity in industrial plant and equipment. Capital expenditures

are expected to increase moderately in the year ahead and will add to that capacity equipment that will help to lower costs and further reduce the need for labor.

Building activity generally has been reduced from the high levels reached in 1959, and there may be some doubt whether a building boom of great proportions could be regenerated even with an increase in the availability of financing and lower long-term interest rates.

The poststrike inventory expansion quickly revealed that stocks of goods were larger than necessary under the circumstances. Although the adjustment to a more normal rate of inventory accumulation may have ended or be approaching an end, only moderate stimulation should be expected from this source in the near future.

Requisites for further maximum and sustainable growth in the economy rest primarily in the selling and pricing policies of business. Demands for the increased supply of goods and services that industry is capable of producing will need to be stimulated by attractive pricing and by offering goods that the public wants. It is to be hoped that growing competition at home and abroad will foster the adoption of such practices. The necessary adjustments, however, will not be easy to make in view of past rising price trends. Failure to make them, and any tendency toward price increases, will be more of a damper on the economy than a basis for expansion.

In the meantime, until demands are stimulated, business profits are not likely to increase much. Continued increases in wages and other labor costs may offset the effects of increased productivity and exert a squeeze on profits. For this reason there should be little reason to fear the resumption of speculative tendencies in the stock market.

Interest rates in the past year reached a level that has encouraged saving and attracted savings into fixed-interest investments. The current level of saving is probably adequate to meet the credit and investment demands that will develop this year. Not only does the current level of interest rates relative to returns on equities put a damper on stock prices, but it may also restrain spending for consumption and encourage certain types of investment. At present there seems to be no reason to force interest rates any higher.

Slackening in the rate of growth in the money supply was necessary during the past year in view of the rapid expansion of the preceding year and the large volume of liquidity being supplied by the issuance of short-term Government securities to finance the deficit. Although these liquid assets are still outstanding, their growth has ceased, and some expansion in money might safely be resumed.

One limitation on credit and monetary expansion, other than the availability of reserves, rests in the reduced

liquidity positions of banks. Although no satisfactory standards are available to measure the possible impact of this factor, there has clearly been a significant change.

This enumeration of existing structural limitations on exuberance is not intended to convey the impression that adequate growth will not occur. Nor should it be interpreted as suggesting that monetary and fiscal policies should be redirected toward increasing buying power or stimulating credit expansion. It is designed merely to indicate that official restraints on the use of credit may be less necessary in the immediate future than they have been at other times of high activity in the postwar period. The situation may change quickly and may even now be in the process of changing. Presently available information and analysis, however, supports the view that the current somewhat more relaxed monetary policy is not inappropriate.

Mr. Marget commented as follows regarding the balance of payments:

At the last meeting of this Committee, I ventured to characterize as "impressive" the improvement in our balance of payments that has taken place since the low point around the middle of last year. There is nothing in the news of the last three weeks to warrant a modification of that judgment. The export figures for the month of March, which are now available in their preliminary form, did not, to be sure, show a "zoom" (as an unfortunate headline in the New York Times suggested) above the already relatively high annual rate of $18-1/2 billion which was represented by the January-February average; but the March figures do show that the relatively high January-February average rate was being maintained. It was on the basis of an assumption that there would in fact be "no great change in exports in March" that I ventured to suggest, last time, that our merchandise export surplus for the first quarter of 1960 would turn out to be at an annual rate of about $3 billion--" just about double the $1-1/2 billion average that we showed during the second half of 1959," which itself was $1-1/2 billion above the low point (a virtual zero surplus in merchandise trade) in the second quarter of last year.

This degree of adjustment in our balance of payments has taken place within a cyclical environment which, as I have been emphasizing, has been of just the kind to favor such an adjustment: a strong demand situation abroad, which is favorable to our exports, and a relatively less intense demand situation here, which would work in the direction of moderating the rate of growth of our imports. But I think that it would be wrong to minimize the significance of the adjustment on the ground that the improvement we have been witnessing has been "merely cyclical"; and this for several reasons.

In the first place, it must be remembered that, in some quarters, our balance-of-payments problem itself has been regarded as a "merely cyclical" problem, which came to us because of a special cyclical constellation and could be expected to disappear when that cyclical constellation changed, as it has in fact been changing. This is a view which I do not happen to share. But it is certainly true that a cyclical element was involved in the deterioration of our balance of payments; and my own view is that a failure to recognize this fact was responsible for some of the excessively pessimistic views that were being expressed when our balance-of-payments deficit was at its maximum. If, now, we have been witnessing developments which attest to our ability to cope with the cyclical part of our problem, this ought to be a source of at least moderate satisfaction.

For--and this is my second point--we should not have been able to deal as well as we have thus far dealt with the cyclical part of our problem if in fact our general competitive position were as hopelessly bad as some of the more extreme pessimists had implied. A strong demand situation abroad means an opportunity to sell abroad, if and to the extent that we are competitive; it does not provide a guarantee that we shall be able to sell abroad regardless of our products' price, quality, and terms of delivery.

Thirdly, there is independent evidence that our producers have not been simply sitting back, with their old lines of wares spread out before them, waiting for a new surge in the cyclical tide of foreign demand to pick them up at the point at which they were left when the earlier tide of foreign demand had ebbed. The most publicized example of this, of course, is the automobile industry, which, after what was undoubtedly too long a period of complacency, finally managed to respond to the challenge of foreign competition in a way which has already clearly affected automobile imports into this country, will affect them even more when the plans for the still smaller cars are implemented, and will undoubtedly be able to affect our exports very significantly, in the degree that we succeed in inducing foreign countries to put no greater obstacles (such as tariffs, quotas, and a whole battery of discriminatory devices) in the way of their nationals buying American automobiles than we now put in the way of our nationals buying foreign automobiles. The automobile is only one example, even if it is the most striking one. Our competitive progress in the field of jet planes is a second example. A third is being provided, surprisingly enough, in the field of electrical equipment, where a combination of a change in pricing policy and a more flexible practice of procurement of components from

abroad when that is economically preferable has produced some unexpected results in a field in which it was supposed we were hopelessly outclassed.

These developments, surely, are more than "merely cyclical." But what has to be stressed, as always, is that improvements of this kind, cyclical or noncyclical, do not come about in a vacuum with respect to general economic and monetary policy. If we have had the degree of success we have had in meeting the cyclical problem, for example, that is because our general economic and monetary policies, oriented though they necessarily were in the direction called for, in the first instance, by the requirements of the domestic economy, have also been compatible with the requirements for continued progress toward a better balance in our international accounts. We are still quite a distance away from a position of "reasonable equilibrium" in our international accounts; it may very well be that, in our further progress toward such a position, we shall have to pass through cyclical phases which will be much less favorable than the current phase obviously is. It would not do to allow our recent successes, in fields relevant to the problem of balance-of-payments adjustment--and they have certainly been successes as far as they have gone--to blind us to the hazards that still have to be traversed on the long road ahead of us.

Mr. Treiber presented the following statement of his views with respect to the business outlook and credit policy:

The most recent business information indicates the probability of a moderate expansion in business activity. The principal uncertainty is with respect to the rate of increase and the timing of the expansion.

Consumer spending shows signs of recovering from the aftereffects of the steel strike and the adverse effects of the unusually unfavorable weather conditions in many parts of the country.

Despite the substantial increase in inventories in the first quarter of 1960, due in large part to the restocking by automobile dealers and steel processors, inventory-sales ratios in manufacturing and trade continue near record low levels. While the rate of inventory accumulation will necessarily decline, especially if inflationary psychology continues low, it seems likely that consumer demand will call for some further additions to inventory for some time ahead.

There are increasing signs that the decline in residential building may be bottoming out. Mortgage funds are becoming more readily available; this is likely to provide considerable support for home building, as demand remains basically strong.

State and local government expenditures are likely to continue their gradual rise. Federal Government spending is expected to expand during the second half of 1960.

Increased plant and equipment expenditures with a high portion for modernization will create a demand for a variety of goods and services.

With the labor force and productivity rising, a substantial reduction in unemployment seems unlikely.

The price picture shows little change, even though the consumer price index and the wholesale price index both rose in March; in each case seasonal influences in the food area accounted for a large part of the rise.

Municipal and corporate bond markets in recent weeks have been more responsive to the better business outlook than the stock market. The flow of municipal securities has increased. There has been some hesitation in the corporate bond markets with investors expecting somewhat higher yields on new issues. After a slow start, corporate securities floated during the first quarter of 1960 came close to the total of the corresponding period a year ago. First-quarter corporate earnings reports are on the whole favorable, although not uniformly so.

The large liquidation of United States Government security holdings and net repayments of security loans in the first quarter of 1960 reduced total bank credit substantially. Yet loans other than security loans rose twice as much as in 1959, although much less than in 1956.

Bank liquidity positions continued to tighten with loan-deposit ratios up and short-term liquid asset ratios down. On the other hand, the nonbank public had higher holdings of liquid assets in relation to GNP than in any quarter during 1959.

The demand upon banks for business loans has continued to be strong all this year, although it has not been as great as some exuberant observers expected at the beginning of the year. Bankers with whom we have talked are expecting the demand for business loans to increase over the coming months.

The Treasury is in the midst of a large refunding operation.

These various factors counsel no significant change in credit policy. We see no reason to change the discount rate, the directive, or open market policy. We think it is no longer necessary to resolve doubts on the side of ease.

Mr. Johns said he would not discuss developments in the Eighth District because he saw nothing in them that was significantly different

from the analysis of national affairs that had been presented. His appraisal of the situation was, he hoped, implicit in the discussion of policy that he proposed to present. Mr. Johns then made the following statement:

> Open market operations since the last Committee meeting have moved quite clearly, I think, in the direction indicated by the Committee. At the April 12 meeting the Committee's consensus called for more reserves to be supplied to the banking system and for the Desk to have authority to permit net borrowed reserves to reach lower levels in order to provide the indicated increase in bank reserves. Data available to me show that total reserves (seasonally adjusted) have risen by about $500 million from the week ended April 13 to the week ended April 27. While this was being accomplished, net borrowed reserves declined from an average of $205 million for the week ended April 13 to an average of $82 million for the week ended April 27.
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> The rate of increase of total reserves over the past two statement weeks was doubtless greater than would be desirable over a long period of time. In the perspective of the last four months, however, such an increase may be regarded as having properly offset in part the decline in reserves since the first of the year. The adjusted reserve total for the week ended April 27 is approximately the same as the seasonally adjusted total for the week ended February 3, but is still roughly $200 million below early January. In the sense of getting back to where we were three months ago, this increase in reserves may be considered, in my opinion, as eminently satisfactory.
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> In the presence of an economic situation currently lacking boom characteristics, I would recommend that total reserves continue to be increased at a moderate rate over the next three-week period. Within the framework of existing operating procedures, this recommendation again carries with it the further recommendation that the Manager of the Account continue to have authority to permit the net reserve position of the banking system to reach whatever level may be necessary to achieve a continued increase in total reserves.
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> The disparity between the discount rate and the bill rate which has prevailed since January continues to place an unnecessary burden on open market operations in the sense that more massive injections of reserves may be required in order to bring about an increase in total reserves. Accordingly, I would favor a reduction in the discount rate at the earliest opportunity. At the moment it occurs to me that the amount of the reduction should be half a point.

As time goes on and business developments are observed, I am brought around to a position stated by others at previous meetings, namely, that clause (b) of the directive needs to be revised so as to eliminate the appearance of single-minded emphasis upon an assumed necessity to guard against excessive credit expansion. I think a guard against too little credit expansion now merits at least a share of the spotlight. But since a policy directive which wars alike against too little and too much is hardly more than a timeless platitude, I am loath to suggest a directive in such terms. However, if the guard against excessive credit expansion is merely deleted from clause (b), there is left only another timeless and self-evident intention, that is, to foster sustainable growth, etc. Therefore, I venture to suggest trying to implement the idea of "fostering sustainable growth in economic activity and employment" by saying in the directive what the Committee expects the Management of the Account to do toward that end at this time. This, of course, will have to await the end of the discussion today and the derivation of the consensus, but if the consensus should be, for example, along the lines of the consensus three weeks ago, it would be appropriate, I think, to say something like "fostering sustainable growth in economic activity and employment by bringing about moderate growth in the total reserves of the member banks." I, for one, would be willing to add to this the further statement: "with a view to encouraging moderate growth in the money supply."

Mr. Bryan presented a statement substantially as follows:

A number of new figures are available for the Sixth District. On the downside, on a month-to-month basis, are nonfarm employment, manufacturing employment, construction employment, bank debits, average weekly hours, manufacturing payrolls, and--of the same significance--insured unemployment is up. Year-ago comparisons in these series tend to be less favorable than they were; and in at least one important series, namely, average weekly hours, both the monthly and yearly comparisons are negative.

On the brighter side is a sharp rebound in department store sales, with some increase in retail sales generally. Also comforting is an increase--for the second successive month--in construction contract awards: a circumstance that would be the more encouraging if awards, even so, were not 22.5 per cent below a year ago.

Most of these figures, of course, apply to March and were substantially affected by weather. The business contacts of the Reserve Bank, and some spot checking, indicate a bit of improvement in April in both business and business sentiment. However, our research department has attempted--on a rather informal

basis, to be sure--to determine if weather can be accounted the sole cause for the uninspiring figures from the District. The conclusion is that the weather explanation does not fit all the facts and that bad weather, although greatly important, has been only a partial explanation of economic events in the Sixth District in the first quarter.

As a sort of "straw in the wind" I will note that our April directors' meeting, for the first time in my memory, received as a result of the Jacksonville Branch meeting a genuinely pessimistic report on the Florida outlook. There can be no doubt that construction in many of the areas of the State has been overdone, and the construction industry is faced with a considerable contraction. Moreover, while the number of tourists in the State seems to be at an all-time high, the expenditure per person is generally said to be notably lower--a point apparently confirmed by banking figures. I note this Florida matter because, while the State may not bulk large in the national economy, it bulks extremely large in the Sixth District: a large part of the District's good showing in the postwar period has resulted from Florida's expansion.

Speaking to the national economic situation:

It does not seem to me that there are clear signs of an economic downturn. By the same token, I see no signs of out-of-hand economic boom; no speculative fever; no effort of the economy to expand at an unsustainable rate. Rather the contrary: the economy seems to have unutilized and growing supplies of manpower, materials, and plant capacity; and I am inclined to think that we may be in the period of slow relative growth generally characterizing the ending phase of an expansionary cycle.

Whatever may be the case as to our position in the cycle, however, the one clear fact, it seems to me, is that the economy is not now expanding at an unsustainable rate. My own conclusion is thus that we can justify a policy that keeps bank credit expansion under control, lest we kindle again the inflationary expectations that have heretofore done the country so much injury; but we must supply the reserves necessary to permit a sustainable growth in the economy.

Thus far in 1960 reserves of the banking system are less than they were at the end of 1959--whether on an actual or a seasonally adjusted basis, and allowing for no growth of reserves at all. Accordingly, I think the banking system, and, through it, the economy, has been under great and, until just recently, increasing restraint. It is clear that I think this restraint has been inappropriate and dangerous.

In the three weeks ending April 27 required reserves have increased massively--by approximately half a billion dollars--and total reserves have increased by an equal amount. Of the

increase in total reserves, a minor amount has derived from the net of System purchases, repurchase agreements, and discounts; and the larger part by far has derived from other factors. What has happened in effect is that we have permitted float and such like items to supply the increase in required reserves.

Attention is called to the derivation of the reserves for a single reason. We shall need to pay close attention to our knitting in the next several weeks, lest the reserve gains we now exhibit disappear in the same way they came. Attention is called to the increase in required reserves to point out that it has occurred in considerable part because of the banks' participation in the Treasury's April financing, and to suggest that, unless we supply reserves, the banks will be compelled to divest themselves of investments and to extinguish the derivative deposits--which is, in my judgment, precisely what we do not want.

Now, with our recent accomplishments in increasing reserve supplies, where do we stand? Well, although in the weeks just past there has been a large increase in total reserves, using daily average figures, there is still a deficit in total reserves of the banking system, through April as compared with December, of $362 million--and on a seasonally adjusted basis allowing for no secular growth of reserves at all. Allowing for even a modest growth from December, seasonally adjusted, the reserve deficiency, of course, is even greater.

It seems to me that the economic and banking situation calls for us resolutely to repair this deficiency--in a minimum order of magnitude approximating $350 million, and then, naturally, to consider where we go from there. I would myself greatly prefer to see this Committee give a very simple instruction in terms of daily average total reserves for the month of May, reconsidering the instruction, of course, at our next meeting. Since the money market repercussions of an attempt to repair the reserve deficiency all at once might be undesirable, I would like to see the Desk instructed to aim in May for daily average total reserves of $150 million more than the daily average of reserves in April of $18,090 million. There is in May a usual seasonal decline of reserves slightly in excess of $50 million. Accordingly, this instruction, if adopted,--and with the full understanding that the Desk is not expected to produce a miracle by hitting the target right on the nose--would have the effect of repairing the reserve deficiency by about $200 million in a one-month period.

On the other hand, if the Committee prefers the infinitely more complex medium of instruction--I refer to net borrowed reserves--I would like to see the target set in a range of $0 to $100 million, with it being understood that the Desk has

latitude to go below this range into the free reserve area in case required reserves show a tendency to decline.

I see no reason to move the discount rate down at this time. I would prefer to see a further reduction in the banks' indebtedness to the System before taking action on the discount rate. I see some merit in the questions that have heretofore been raised, and that Mr. Johns raises at this meeting, with respect to the directive.

Mr. Bopp summarized the Philadelphia Reserve Bank's spring survey of Third District manufacturers regarding plans for plant and equipment expenditures, which indicated total estimated expenditures of $410 million, up 15 per cent from expenditures last year and up 8 per cent from expectations last fall. The estimated total would represent an all-time high. On an industry-by-industry basis, the results of the survey fairly well paralleled other surveys except for a significant decline in petroleum expenditures. Philadelphia manufacturers anticipated that employment would be up about one per cent in the second quarter but would return to present levels by the end of the year, and views on production were similar. Whereas last fall most of the respondents expected some increase in inventories, at present as many expected a decline as an increase.

With further reference to the Third District, Mr. Bopp said that activity was fairly satisfactory except for steel production. Employment was better than a year ago, particularly in the hardest-hit areas of the District. Builders reported more people looking at homes than at any time in their experience, but sales were said to be sluggish.

Mr. Bopp expressed some concern about capital market developments, as reported on page 25 of the staff memorandum on the economic and financial situation distributed under date of April 29, 1960. In view

of the continuing amount of unemployment and the extent of idle productive capacity, the slow movement of corporate and municipal bonds through the capital market was not reassuring. While he would not suggest that the Federal Reserve move into the longer-term market, Mr. Bopp felt it would be appropriate to try to prevent any appearance of tightness in the short-term market. For the next three weeks, it seemed to him that the System should make reserves available to take care of any deposits arising out of loan expansion so that the banks would not have to liquidate Government securities or come to the discount window. He would have sympathy with the views expressed by Mr. Johns on the policy directive, and possibly on the discount rate except for the fact that a period of Treasury financing was now in process. In the circumstances it would not seem appropriate to act on the discount rate at the next meeting of the Philadelphia directors, but action might seem in order after the ensuing two-week period.

Mr. Fulton said that the only good news from the Fourth District was in connection with consumer takings. Department store sales were strong over the Easter period and at the end of that period were 5 per cent ahead of last year. The department store people felt that the level of sales reflected a desire for goods more than unusual circumstances due to weather conditions and the late Easter date, and they anticipated quite a good year as far as consumer takings were concerned. New car sales also had increased quite sharply. Insured unemployment was down throughout the District generally, except in some cities closely

connected with the steel industry. Building activity picked up substantially in the Cleveland area in April, and to a lesser extent in the Cincinnati area, with the improvement largely in nonresidential construction.

Steel operations continued to decline, Mr. Fulton said, and for the District this week's estimate was 72 per cent of capacity against 74.8 per cent for the nation. The steel mills reported that cancellations were high and that they were shipping more than was being ordered. Even with the pickup in auto sales, it was felt that orders were going to be low almost into September, and that a substantial amount of inventories apparently was being worked off. Reports from the foundries that supply the appliance field were similar. The situation in the machine tool industry was spotty, but new orders were looking up. In summary, the steel industry felt that the low point had not yet been reached and that the national rate might go below 70 per cent of capacity in this quarter, with no material pickup until almost the fourth quarter. Shipments of pipe and wire from foreign sources were said to be demoralizing American production. However, there had been some increase in the shipment of sheets out of the country because European countries apparently were using more than their capacity to produce.

With regard to the financial picture, Mr. Fulton reported that bank loans were up, savings deposits had reached an all-time high, and borrowing from the Reserve Bank was moderate. He felt, however, that the liquidity of banks had been reduced to such an extent that an increase in the availability of reserves would be quite appropriate.

Accordingly, he would like to see the level of net borrowed reserves reduced to around $100 million or less. He would favor postponing a change in the directive and, temporarily at least, he would not be inclined to adjust the discount rate.

Mr. King recalled that when he became a member of the Open Market Committee about a year ago the economic indicators were generally pointing upward. Today, however, the picture was different, and many of the indicators were pointing downward. With reference to the unemployment situation, he described how, at a plant in the southeastern part of the country with which he was familiar, there had been a substantial reduction in the number of employees along with a reduction in working hours and management was now considering a further reduction of force in order to increase working hours and retain the more efficient employees.

Mr. King recalled that earlier in the year he had expressed concern regarding the trend of corporate profits. Apparently, he said, there was still need for concern, because it seemed clear from the historical record that recessions are forecast by a continuing decline in corporate profits. From a reading of the minutes of the Committee meeting on April 12, he noted that apparently there was quite a bit of concern about taking any action that would suggest doubt as to the System's belief in the underlying strength of the economy. While that was a point worth considering, he did not believe that a reasonably small move in a direction of less restraint would cause the economy to go into a tailspin. Instead, a failure on the part of the Open Market Committee

to recognize the facts of the situation seemed more likely to cause the economy to go into a downturn. While he did not believe that the country was in a recession, he thought it possible that a recession might develop in a reasonably short time. One problem, as he saw it, was to destroy the idea that if the System moved in a certain direction the whole economy was going to go in that direction. The psychology seemed to be that when the System was exercising restraint the economy was fine, and that when the System moved toward less restraint things were going badly. It was important, he suggested, to destroy that kind of thinking, and this seemed a good time to try to accomplish that objective.

Mr. King said that he would be agreeable to supplying reserves along the lines suggested by Mr. Bryan, although he did not comprehend completely all of the details of Mr. Bryan's system. In terms of net borrowed reserves, he would consider a range of from zero to $100 million appropriate as a target.

Mr. King agreed with the view of Mr. Johns that it would be appropriate to remove from the directive the phrase "while guarding against excessive credit expansion." This was not of too great importance, but it would indicate that the Committee was as alert to weaknesses in the economy as to strength. He would be inclined to approve a reduction in the discount rate of 1/2 point if a majority of the Reserve Banks wanted to move on the rate.

Mr. Shepardson said that he had been concerned about a possible recurrence of the fever that was in the air at the beginning of the year.

However, it seemed to him now that the economy had passed that period and today his views were much like those expressed around the table thus far. In view of the lack of real strength in a good many areas and definite lack of strength in other areas, perhaps the System should be easing further than it had to date. There seemed to be a need for further expansion of the money supply, or rather a rebuilding of the contraction that had taken place earlier. Therefore, he would favor a further increase in the supply of reserves.

Mr. Shepardson felt that the point that had been made regarding the directive was well taken, and that the phrase "guarding against excessive credit expansion" could be eliminated. He had no wording to propose, but would be willing to go along with the idea expressed by Mr. Johns. As to the discount rate, it seemed to him that the time might be approaching when the rate should be changed. Since the Treasury financing would extend through a substantial part of the period until the next Committee meeting, an immediate change in the rate might not be appropriate, but, depending on interim developments, such action might seem in order by the time of the next meeting.

Mr. Robertson commented that those who had spoken thus far seemed to be putting all the weight on unfavorable factors when just as many factors were favorable. As he reviewed the economic picture during the past few months, he felt that the policy followed by the Committee had been pretty nearly right, and he saw no reason at the moment to change policy. He did not believe that this was a time for making errors on

the side of ease, although he would not advocate tightening or adding to restraint. In his view, this was a time for the System to be almost neutral, and thus be in a position to move in either direction. Looking at the economic indicators, he felt the chances were greater that the economy would move upward than that it would move downward. Consequently, although he would not seek greater restraint at the moment, neither would he seek greater ease.

Mr. Robertson went on to say that for the moment he would not favor a change in the discount rate. He might come to the point where he would favor such a change in the relatively near future, but he was not certain. Neither would he favor a change in the directive at this time, for he felt that the System was still in a position of having to guard against excessive credit expansion. Credit demands were heavy, and apparently would continue to be heavy. As to the liquidity position of the banks, he felt that the current situation was desirable because it placed the System in a position where it could exert a greater impact on the economy than would otherwise be the case. In summary, he would leave things pretty much as they now stood for the forthcoming three weeks.

Mr. Leach said that economic activity in the Fifth District, reinvigorated by a spring pickup in most retail markets and by the year's first substantial batch of new orders received by mills for cotton cloth, had continued at a high level. There was no evidence, however, that the recent business improvement was more than seasonal. There were enough soft spots in the over-all business situation to cause businessmen to

pursue conservative purchasing and inventory policies and to view prospects with cautious optimism. Circumspect policies were apparent at the spring furniture market in North Carolina, which was marked by good attendance, the showing of many new lines, and considerable interest on the part of dealers. Nevertheless, sales were not heavy. Dealers apparently were unwilling to carry anything but the bare minimum of inventory since most items could be obtained quickly from manufacturers' stocks and no price advances were anticipated in the near future. In line with earlier estimates of increased capital outlays this year, construction firms reported that there was plenty of business; however, profit margins of most contractors were down sharply. In fact, competition among contractors bidding for a given job has been so severe in some cases that successful bid prices were below cost estimates. Evidence that pressures on member banks continued to be strong was provided by higher than seasonal borrowings from the Federal Reserve Bank and by the fact that Fifth District member banks were net purchasers of Federal funds in each of the past three weeks.

With respect to policy, Mr. Leach said that he thought the Committee was about where it should be and that he would recommend maintaining substantially the position achieved in the past three weeks, resolving doubts on the side of ease. As to net borrowed reserves, he had in mind a figure around $150 million as a benchmark. Such a level seemed consistent with current economic conditions, and he would not want it higher. Now that loans and investments and required reserves were again expanding,

maintenance of a fixed level of net borrowed reserves would presumably mean purchases of securities to provide additional reserves to support growth in the economy. In any event, the current Treasury financing called for an even-keel policy for the immediate future.

Mr. Leach noted that he had spoken in the past in behalf of an improved technique in handling the directive. Inasmuch, however, as the old form was still retained, he had recommended at the last meeting elimination from the directive of the expression "while guarding against excessive credit expansion." Believing that the Committee should be more flexible with respect to the directive, he would remove the expression now, although its elimination would have been more timely three weeks ago. He saw nothing in the remarks of Messrs. Noyes and Thomas that called for guarding against a booming credit expansion in the near future. He would not favor a change in the discount rate at this time.

Mr. Leedy said that available Tenth District statistics indicated trends quite similar to national trends. Prospects for the winter wheat crop continued to be good despite the severe winter weather; in most parts of the District the condition of the wheat was reported from good to excellent. As of the first of April, the Department of Agriculture anticipated that the wheat output of the District this year would be approximately the same as last year.

With respect to policy, Mr Leedy expressed the view that the Committee had not started too soon in making additions to reserves. Weighing the substantial number of favorable indicators against the

unfavorable ones, it seemed to him that some further active participation by the System in the direction of making reserves available for needed expansion was a proper course to follow. While he would not want to do anything dramatic in that direction, he felt that the course the Committee had embarked upon should be continued, with net borrowed reserves trending downward.

Mr. Leedy noted that the existing discount rate was fixed at a time when the System was aggressively attempting to exert restraint, and that such a policy was not called for at present. In view of the action taken with respect to providing reserves, it did not seem to him that the discount rate level was quite appropriate; he thought this was indicated by events in the past few weeks. Therefore, he would favor a reduction in the discount rate of 1/2 point as soon as that could be done in the light of the Treasury financing. In this connection, he noted that a number of the Reserve Banks would have meetings of their directors on the second Thursday of this month, after which there would be no other regular meetings until the same time in June, too late to do the kind of thing that he thought was required quite promptly. Since a rate reduction was involved, rather than an increase, he assumed that the period of equilibrium called for by the Treasury financing might be shorter than would otherwise be the case. He thought there was a minimum of danger that a rate reduction would be regarded as reflecting an adverse appraisal of the economy because short-term rates on Government securities had declined so sharply and were now so far out of line with

the discount rate. The suggestion of Mr. Johns regarding the directive appealed to him, and its adoption would be in line with the kind of program that he (Mr. Leedy) had indicated he would favor.

Mr. Allen reported that unemployment compensation claims for the first three weeks of April were substantially higher in Iowa, Wisconsin, and Michigan than last year. The cutback in automotive employment had begun to result in layoffs rather than merely a reduction in hours of work. Recently, layoffs had been reported also in farm machinery, construction machinery, and household appliances.

The optimism in Detroit that he reported three weeks ago continued to prevail, Mr. Allen said. The daily sales rate for the last ten-day period of April was believed to have exceeded 23,500, which would mean sales of 580,000 in April. Production in April probably equaled 580,000 so inventories undoubtedly remained above 1,000,000 units. Manufacturers prefer, of course, to continue to produce at a steady, high rate because of the economies involved, and at the same time the improved sales made them disposed to gamble that sales in the weeks ahead would accomplish the dual task of covering current production and reducing the high inventories.

In steel, the operating rate in mid-April was just under 80 per cent for the nation, whereas it was 85 per cent in the Chicago area. The rate in Detroit had been erratic but generally well above the national average. Department store sales in the Seventh District were

strong, with the year-to-date improvement about the same as reported for the nation.

Chicago money market banks had recovered the deposits lost over the April 1 tax date, and their reserve position had improved markedly since a month ago. However, they were still borrowing, at the discount window and in the Federal funds market, this being attributable largely to participation in recent Treasury financing operations.

Mr. Allen commented that he liked the phrase "lean against the wind." Right now, however, it did not seem that there was much, if any, wind. Recent developments, particularly the strength of retail trade in March and April, seemed to have dispelled the concern that a recession might be in process or imminent. However, most forecasts indicated that the rise in aggregate demand in the months ahead would not be sufficient to press upon the available supply of labor and productive facilities. As he saw it, business was good but was running scared, which was not a bad way for it to be.

For the moment, therefore, Mr. Allen felt that there was little point in leaning either way and that the System could pursue a neutral course. On that basis he would not object to seeking a zero position on reserves, neither net borrowed nor net free. He would not favor a change in the discount rate at this time. Quite aside from the current Treasury financing, which argued for an even-keel position for the next few weeks, he did not think other factors were such that he could support a lower rate now. Three weeks hence could be another story. He

felt the same way on the policy directive; for the reasons stated by Mr. Robertson, he would continue to include the phrase "while guarding against excessive credit expansion."

Mr. Deming said there were two points about the Ninth District that might be noted. First, there was optimism in the farm areas of the Dakotas and Montana about crop prospects, mainly because of favorable moisture and planting conditions. Second, the District might be witnessing the ending of an unusually deep seasonal deposit decline. Country bank deposits and city correspondent balances had increased in the past two or three weeks. The banks were still pressed hard for liquidity, however. Relative to a year ago, their loans were up $250 million. In effect, they had financed this loan increase by an equivalent liquidation of Government and other securities, and at the same time they had had to accommodate themselves to a $250 million deposit loss.

At the national level, Mr. Deming said, the general economic picture, as he saw it, was not particularly impressive or depressive. Mr. Bryan's characterization of the economy as not expanding at an unsustainable rate expressed his own feeling very well. Thus, he saw no reason to take any drastic action to change policy. At the same time, he saw no danger in following a mildly easier policy with respect to bank reserves, perhaps aiming at a zero level for net borrowed reserves, as suggested by Mr. Allen. He would prefer to wait on any discount rate change, and he would not change the directive at this time.

Mr. Mangels reported that developments in the Twelfth District were rather mixed. Employment increased in March by a fraction of one per cent, mostly in the food processing plants, but unemployment also was up a fraction of one per cent, reflecting reduction of personnel at aircraft plants offset to some degree, in California, by increased employment at electronic plants. In the first three weeks of April, steel production was at 74 per cent of capacity against 80 per cent for March. Some steel companies had reduced prices on certain items, with discounts running as high as 11 per cent on items subject to intensive foreign competition. Total construction was up, with all of the increase in the nonresidential category. In the first quarter of 1959, residential vacancies in the West increased to 9.7 per cent compared with a rate of 8.3 per cent in the fourth quarter of 1959. After making allowance for the later Easter, department store sales for the year to date were about even with last year; sales for the four weeks ended April 23, unadjusted, were up 8 per cent from the same period a year ago. Automobile sales in California were 12 per cent over a year ago in March, and the improvement was continuing in April. Reports were heard that sales of compact cars and expensive cars were strong, while the intermediate-price models were a drug on the market.

Mr. Mangels went on to say that Twelfth District banks increased their holdings of Government securities by $300 million in the three-week period ended April 20, and that loans increased about $265 million in

the same period, with increases in all classifications except real estate loans. Demand deposits were up more than $500 million from March 30, and time deposits showed a modest increase, but savings deposits declined about $34 million. Bankers, particularly those representing the larger banks, were quite concerned about the continued loss of savings deposits and expressed the view that they could not recover the deposits they had lost, or halt the continued decline, unless something was done about the maximum permissible rate of interest. Borrowings from the Reserve Bank were scattered and on a nominal basis, while District banks were net sellers of Federal funds.

With respect to policy, Mr. Mangels observed that apparently little could be done in the next week or two in view of the Treasury financing. He noted that net borrowed reserves averaged $82 million for the latest statement week, and his inclination would be not to go above that figure. In fact, if it were feasible and practicable, he would be inclined to go lower, perhaps even to a zero basis. He saw no harm in going lower at this time for there seemed to be no steam in the boiler at present. The growth of retail sales had been small, the decline in steel production was rather extensive, the steel industry did not seem to expect any major change in that situation, and there had been an increase in unemployment. Reports were seen in the press of layoffs in manufacturing establishments and, although those reports were scattered, they might be indicative of a trend. In the Twelfth

District, price-cutting with respect to autos, home appliances, and other commodities had been observed. Generally speaking, business had been good thus far, but there was considerable concern about what the rest of the year was going to bring and it was not unusual to be asked whether the country was heading toward recession. With that as background, it appeared to him that the System could afford to be somewhat on the easier side without damage to the economy, and the directive seemed broad enough to permit such a course.

Mr. Mangels felt that perhaps it would not be appropriate to make a change in the directive today, and he had the same feeling with regard to the discount rate. The next meeting of the San Francisco directors was to be held on Thursday, May 5, and the directors then would not meet again until the first Thursday in June. At present, it was his thought to recommend to the directors that no change be made in the discount rate.

Mr. Irons stated that conditions in the Eleventh District were quite satisfactory and that the major factors had not shown much change. Department store trade moved up sharply in the past month and the totals were running a little ahead of last year on a cumulative basis. Nonfarm employment had increased about seasonally, while unemployment had decreased in about seasonal proportions. Construction activity had moved upward during the past three weeks, with residential construction accounting for a good part of the gain; the greatest strength in construction activity appeared to have shifted from the Dallas area to the

Houston area. The petroleum situation continued unchanged; allowables were dropped back to eight days for the current month and probably would continue on that basis. However, there were no signs of great despair in the industry, which recognized that it had a problem and was facing up to it. Some increase was noted in drilling activity within the past month. The industrial production index for the District was down a point due to the petroleum situation. With good weather prevailing recently, the agricultural sectors of the District were encouraged. While cash farm income was about 6 per cent under a year ago, the outlook for current crops was good.

On the basis of recent visits with bankers and others around the District, Mr. Irons said that on the whole conditions appeared to be generally satisfactory. There was no sense of boom or surging activity, but he got no feeling of pessimism. On the financial side, there had been increases in total bank loans, business loans, and consumer loans over the past three weeks. The banks had added to their investments in connection with their participation in Treasury financing. Deposits had turned upward and showed a sizable increase in the past three weeks. City banks indicated that they were still loaned up, that loan demand was strong, and that they were being selective in granting credit. Borrowing from the Reserve Bank had increased somewhat and was in about the usual percentage relationship to the System total. Federal funds were being used in substantial amount, mostly by a few of the larger banks with high loan-deposit ratios and no bills to sell.

With regard to the national picture, Mr. Irons indicated that he leaned toward the views expressed by Mr. Robertson. Some of the current developments in the economic field appeared to be in the nature of inevitable adjustments, and the economy might be getting on a sounder foundation than if the earlier rate of expansion had continued longer. In steel and autos, for example, it could not be expected that there would be additions to inventories at the earlier rates over a very long period of time. In fact, the economy might be moving toward the growth and stability that the System had been seeking rather than the other type of development that appeared earlier to be in prospect. While he did not foresee a surge upward, neither did he see points of basic weakness that were likely to lead to serious economic difficulties. In these circumstances, while he saw no need for greater restraint, he saw no need for greater ease.

Mr. Irons indicated that he would not favor a change in the discount rate at this time. The rate was only out of line with the bill rate, and if the System always tried to keep the discount rate in line with the bill rate it would be likely to have trouble. If one looked at other short-term rates, quite a good alignment was found. In this connection, Mr. Irons said that he had usually thought of the Treasury bill as a bank instrument offering an alternative approach to the discount window. Now, however, the bill was hardly a bank instrument; he had noticed recently that less than 10 per cent of the outstanding 91-day bills were owned by banks. This raised some question as to the

significance of the discount rate being out of line with the bill rate at the moment.

Mr. Irons also said he would not favor a change in the directive, although he did not particularly like the wording that related to guarding against excessive credit expansion. With the Treasury in the market and the economic situation as he saw it, he would favor continuing the existing open market policy. He would not set any particular goals for the Account, but he would instruct the Desk to come as near to the conditions of the past three weeks as it could.

Mr. Erickson said that the situation in the First District differed only slightly from the national picture. Nonfarm employment was up in March, but only to the same extent as nationally; on the other hand, insured unemployment was up a fraction of one per cent for the most recent week. This was the second week this year that the figure was higher than a year ago. Construction contracts showed an increase of 2 per cent in March, due primarily to nonresidential construction being up materially. For the year to date, construction contracts were 6 per cent below a year ago. March was the first month when residential contracts were down in comparison with last year, and for the first three months of the year they were up 9 per cent. Department store sales reflected very good Easter business and were continuing satisfactorily, while auto sales also were favorable. District banks continued to purchase Federal funds on balance, and borrowings at the discount window in April averaged just under $25 million, or between

2 and 3 per cent of the System total. A survey of capital expenditures conducted in collaboration with the McGraw-Hill survey indicated that District manufacturers expected to make total expenditures of $634 million in 1960, which would represent an increase of 12 per cent from 1959. Durable goods manufacturers expected to spend 22 per cent more than last year, and manufacturers of nondurables expected to spend 3 per cent more.

As to policy, Mr. Erickson said he wished to associate himself with the view expressed by Messrs. Robertson and Irons that the System should continue to maintain a neutral position. He would favor postponing any action on the discount rate or the directive at least until the next meeting of the Committee. With respect to open market operations for the next three weeks, he would give the Desk the same instruction as at the April 22 meeting.

Mr. Szymczak commented favorably with regard to open market operations during the past three weeks and expressed the view that a significant contribution had been made by the presentations of Messrs. Johns and Bryan. He went on to say that although he would favor supplying some additional reserves to the banking system in such fashion as to bring the level of net borrowed reserves to $100 million or below--down to zero if necessary--he would not suggest that this be done quickly. Obviously, there was not the exuberance in the economy that was anticipated earlier. However, this was only the first week of the second month of the second quarter of the year, and the Treasury was

now in the market. Therefore, he would be inclined to move slowly. He would not favor changing the discount rate or the directive at this time.

Mr. Balderston said that although he considered the description of the state of the economy given by Mr. Bryan an excellent one, he had come to the same general conclusions as expressed by Messrs. Leach and Allen with respect to policy. Continuing, he observed that projections for plant and equipment expenditures included a contemplated 70 per cent increase in expenditures for equipment. This would tend to accentuate the problem of unemployment and at the same time productive capacity, now excessive, would be expanded somewhat. On the other hand, there would be the beneficial result that the adequacy of supplies would diminish the inducement to build up inventories for protective reasons. Also, excess capacity would provide a brake on increases in the prices of tangible goods. When he looked at services and unemployment jointly, he was concerned about what might lie ahead during the next few years. Prices of services doubtlessly would continue to rise, while unemployment had not receded to the extent that one might have hoped at this stage of cyclical expansion. Ahead, therefore, might lie what had been referred to as the dilemma of central banking: rising prices of services and rising unemployment.

Mr. Balderston indicated that he would favor a change in the directive such as Mr. Johns had suggested. The monetary policy that he would favor might be described as one of reluctant ease, the implementation of which would embrace continuation of the present discount rate.

If the Treasury bill rate remained considerably below the discount rate, the differential would, of course, induce banks to sell Government securities, to the extent that they had such securities in their portfolios, and to operate in the Federal funds market. Such a tendency would not seem inappropriate to him because it would tend to relieve the pressure on the discount window. It would call, however, for open market action in the direction of a net borrowed reserve target of zero. In summary, as long as the discount rate was above the bill rate and as long as there was no real evidence of a change in the active money supply, he felt that the Committee should move toward a lower level of net borrowed reserves. He would rather place the stress on open market operations than force increased use of the discount window.

Chairman Martin said that upon rereading the minutes of the Open Market Committee beginning with October 1959, he found them interesting and encouraging. In the past several months, as noted in the minutes, he had from time to time expressed an optimism that he certainly did not feel a year ago, for at that time he did not see the answers to a number of problems. He now saw answers to some of the problems in the financial field and a reasonable expectancy as to their solution. Federal Reserve policy, he felt, had been about right.

At the present time, Chairman Martin commented, the System ought to be struggling for stability. While he did not feel that anyone could know what the economy was going to do, he saw reason for optimism. Some concerns were in financial trouble in the midst of good business, as is

always true in a period comparable to the present. Some concerns had overexpanded, for example, and financing had not yet been found. By and large, however, the economy seemed quite solid.

The Chairman noted that Mr. Mills had for some time raised questions about the level of reserves. He (Chairman Martin) also had had some question on this point since the turn of the year. After commenting on the difficulty he experienced in understanding the money supply, the Chairman said that at the present time he saw no reason why the System should not be supplying more reserves to the market, adding that in saying this he had in mind the longer trend. He would disagree with Mr. Treiber's analysis only to the extent that he (Chairman Martin) felt that the System should be resolving doubts on the side of ease. As he saw it, nothing had changed in the past six weeks to cause the System to resolve doubts on the side of tightness. There had been a long period of decline in the money supply and at the same time a real change in the exuberance of the economy. Thus, all of the odds seemed to be in favor of supplying more reserves.

The Chairman said he felt strongly that it would be a mistake to change the discount rate at this time. A change in the rate would be a dramatic overt action indicating to many people that the System had made up its mind that a basic change in the economy had occurred. Personally, he was not ready for that.

With regard to the question that had been raised regarding the directive, the Chairman indicated that he did not consider the matter

terribly important one way or the other and that much depended on how one read the language of the directive. It could be said that the System always guards against excessive credit expansion, and it could be that unsound credit expansion would develop in the future. In this connection, he pointed out that the directive is not made public until published in the Annual Report of the Board of Governors. Although he had argued at times on both sides of the question, basically he did not think that the language of the directive was terribly important unless the Committee was making a basic change in policy.

Chairman Martin expressed the view that the most recent Treasury financing had been well handled. He went on to comment that Treasury activities had for some time been complementary, if not supplementary, to monetary and credit policy; debt management policy and monetary policy had been working closely together.

The Chairman said that he would like to see in the next three weeks a general approach on net borrowed reserves of trending toward the zero level. With the start provided by Mr. Bryan, studies were in progress with a view to the possibility of developing a better concept than net borrowed reserves, and it was hoped that additional material would be available before too long as the result of work at the Board and elsewhere. Using the net borrowed reserve target, however, it seemed to him that a trend toward zero would be in order at the present time. In his judgment, that would not call for any change in the directive or

the discount rate. There would be another meeting of the Committee on May 24, and things might then be clearer; at that time, the thinking might be in terms of changing the discount rate and amending Federal Reserve policy. However, it seemed to him that any such action would be premature at the present time and that the System should take all the time it could to be sure that System policy was adjusting itself. What impressed him was the gradual evolution of thinking on the part of the Committee that had taken place. From January 12 to the present date, there had been a steady evolution of Federal Reserve policy largely molded by the economy itself, and this had been a satisfactory way for things to develop. However, there was enough uncertainty in the economy today so that it would not seem premature to supply some additional reserves to the market, and there would be little likelihood of generating any real speculative enthusiasm by supplying reserves in a modest way.

Chairman Martin noted that some differences had been expressed during the discussion today, which was a healthy situation. Within the Committee there appeared to be a slight majority in favor of continuing the present directive without change, while a large majority favored a decrease in the level of net borrowed reserves and no change in the discount rate. If anyone wished to record a vote, that would be in order, but it seemed to him that the general discussion had fairly well evolved into a satisfactory guide for policy without anyone having to take a strong stand.

Continuing, the Chairman said that his approach to the relationship between the discount rate and the bill rate was similar to that stated by Mr. Irons. The fact that there were now three-month bills and six-month bills in the picture had changed the situation a little. Generally speaking, it occurred to him that it would be well for the System to stay steady in the boat until it was absolutely certain that a wind was blowing. This point had been brought out well by Mr. Allen. He (the Chairman) did not know where the wind was at the moment, but the reserve position was such that the odds seemed to favor what he understood to be the view of the majority; namely, that the trend of net borrowed reserves should be toward zero. If the reserves were not used, the Committee could quickly reverse itself, whereas a change in the discount rate could not be reversed quickly. In summary, he would maintain maximum flexibility at the present time, yet be moving in line with the way that the economy had developed.

The Chairman then said that unless someone wanted to record a vote he would favor accepting as the consensus of the Committee until the next meeting moving in the direction of lower net borrowed reserves. While it was not too desirable to specify figures, he would favor trending toward zero with the understanding that this did not mean that the Desk had to get there in three weeks or anything like that. As to the policy directive, he understood it to be the consensus that there should be no change at this time. The discount rate is not the subject of decision at Open Market Committee meetings, but it appeared that the

majority view clearly was against action on the discount rate before the next meeting of the Committee. He did not know what the Board of Governors would do if any Reserve Bank should come in with a change in the discount rate, and he did not want to deter any Banks from doing so if they desired; if this happened, the responsibility would be on the Board of Governors. However, he wished to express himself personally as questioning very much whether the Board of Governors should approve a change in the discount rate in the near future.

Chairman Martin then asked whether there were any further comments, and none were heard. Accordingly, he stated that the directive would be approved in its present form and that the comments of individual persons would, of course, be included in the minutes.

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 fostering sustainable growth in economic activity and employment while guarding against excessive credit expansion, 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.

Chairman Martin then referred to the action taken by the Federal Open Market Committee at its meeting on April 12, 1960, authorizing the acquisition, in the period between that date and the next Committee meeting, of up to $150 million of one-year Treasury bills maturing July 15, 1960, either by outright purchase or by swapping other Treasury bills.

The activities of the Desk under this authorization, which resulted in the acquisition of $10 million of July 15 bills against swaps or offsetting sales of a like amount of other bills, were reported in detail in a memorandum dated May 2, 1960, from Assistant Vice President Larkin of the Federal Reserve Bank of New York. The memorandum was distributed to the Committee prior to this meeting with a transmittal memorandum from Mr. Rouse of the same date. Copies of both have been placed in the files of the Committee.

Chairman Martin made the comment that he considered Mr. Larkin's memorandum an excellent summary of developments, following which Mr. Treiber said that in the opinion of the New York Bank the experience under the authorization given by the Committee on April 12 had been satisfactory and continuation of the authorization would be warranted.

It was noted at this point that some of the members of the Committee had not yet had an opportunity to review Mr. Larkin's memorandum fully. Accordingly, Mr. Rouse presented a rather detailed statement of developments under the Committee authoritization, his comments being based largely on the memorandum that had been distributed. Mr. Rouse also said that it had been obvious to all concerned that there were swaps involved in the transactions undertaken pursuant to the authorization, but that, as far as he knew, there had been no comment at all in the market. The transactions had all been accomplished at market prices and without any market repercussions having come to his attention.

Chairman Martin said that he had heard of no repercussions in the market. He went on to say that since an experiment was involved, he would suggest the preparation and distribution of another report along the lines of Mr. Larkin's memorandum if the April 12 authorization should be renewed. He then proposed that the April 12 authorization be renewed for another three weeks from this date, adding that by that time the Committee should be able to view the experiment in a better perspective.

Mr. Robertson said he would like to be recorded as voting against renewal of the authorization, for reasons of principle that he had expressed at the meeting on April 12 with regard to swap transactions. He added, however, that in his opinion the Desk had done a good job in treading lightly and carefully in this field which involved an experiment.

Thereupon, with Mr. Robertson dissenting, it was agreed to renew until the next meeting of the Open Market Committee the authorization given at the meeting on April 12, 1960, to acquire for the System Open Market Account, either by outright purchases or by swaps of other bills, up to $150 million of one-year Treasury bills maturing July 15, 1960.

Chairman Martin then referred to a letter from Under Secretary of the Treasury Baird dated April 13, 1960, requesting the views of the Open Market Committee on an enclosed draft of circular under which refunding securities would be offered for either cash or maturing securities but no special subscription privilege would attach to the maturing securities. In the event of oversubscription, there would be allotments. Although it was not so stated in the proposed circular, the Under Secretary's letter stated that the Treasury contemplated that subscriptions from the Federal Reserve System, Government investment accounts, and all subscriptions up to a minimum amount would be allotted in full. In subsequent discussions, the Under Secretary had indicated that it was the intention of the Treasury to allot in full all subscriptions, irrespective of amount, made by certain other subscribers who would constitute a substantial group, including, for example, State and local governments, foreign governments, foreign central banks, international institutions, and publicly administered pension funds.

A draft of reply and a revised draft had been distributed to the members of the Committee prior to this meeting. With the first draft there was also distributed a memorandum dated April 15, 1960, from the

General Counsel of the Open Market Committee expressing the view that acquisitions by the Federal Reserve Banks pursuant to an arrangement such as described by the Under Secretary would not be subject to the $5 billion limitation contained in section 14(b) of the Federal Reserve Act, which states that "the aggregate amount ...of obligations* acquired directly from the United States which is held at any one time by the twelve Federal Reserve banks shall not exceed $5,000,000,000." The revised draft of reply indicated that the Open Market Committee had reached such a conclusion and that furthermore, since it was contemplated that a substantial group of other investors would be eligible to refund on the same basis as the Federal Reserve Banks, the objection indicated by the Committee to a somewhat similar proposal of the Treasury in 1958 did not apply. (In 1958 the Committee had strongly questioned the advisability of a debt management move that would distinguish in any way between the securities held by the Federal Reserve Banks and the securities held by other investors.) The proposed reply would conclude with the statement that, subject to usual questions regarding monetary and credit policy and the terms eventually set for the refunding security, the Federal Reserve Banks would be prepared to consider refunding some or all of their maturing securities under such a proposal.

In reply to a question by Chairman Martin as to whether there were comments on the matter, Mr. Treiber suggested certain changes in the revised draft of reply to the Under Secretary and stated reasons in support of those suggestions.

* Should read: amount of ... obligations

There being no further comments, it was agreed unanimously that a letter in the form of the revised draft distributed under date of April 26, 1960, as modified to take into account the suggestions of Mr. Treiber, should be sent to the Under Secretary of the Treasury in reply to his letter of April 13, 1960.

Secretary's Note: The letter sent over the signature of Chairman Martin to the Under Secretary on May 6, 1960, pursuant to this action was as follows:

Your letter of April 13, 1960, requests the views of the Federal Open Market Committee on an enclosed circular under which refunding securities would be offered for either cash or maturing securities, but no special subscription privilege would attach to maturing securities. In the event of over-subscription, there would be allotments. Your letter also states that you contemplate that subscriptions from the Federal Reserve System, Government investment accounts, and all subscriptions up to a minimum amount would be allotted in full. In subsequent oral discussions you indicated that it is the intention of the Treasury to allot in full all subscriptions, irrespective of the amount, made by certain other subscribers who would constitute a substantial group, including, for example, State and local governments, foreign governments, foreign central banks, international institutions, and publicly administered pension funds.

Presumably the Treasury circular would state that all subscriptions by such a group would be allotted in full; it seems to the Committee that it is important that the market be so informed in order to be able to evaluate the offering and the prospects of allotments to others.

The question arises whether, under such a refunding offer, the Federal Reserve acquisitions of the refunding securities in exchange for the maturing securities would be "acquired directly from the United States" within the purview of section 14(b) of the Federal Reserve Act, which provides that "the aggregate amount ... of obligations* acquired directly from the United States which is held at any one time by the twelve Federal Reserve banks shall not exceed $5,000,000,000."

A substantially similar proposal was presented by the Treasury for the Committee's consideration in early October 1958. In a letter dated October 21, 1958, the Committee took the position that acquisitions by the Reserve Banks pursuant to such a refunding arrangement would not constitute a direct acquisition from the United States within the meaning of section 14(b).

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* Should read: amount of ... obligations

> Although the Committee's letter did not so state, the Committee strongly questioned the advisability of a debt management move that would distinguish in any way between the securities held by the Federal Reserve Banks and the securities held by other investors, and with your letter of October 24, 1958, you suggested a modified proposal under which there would be no difference in any respect in the treatment accorded the Federal Reserve System as compared with any other investor. To that proposal, the Committee responded that it had concluded that acquisitions by the Reserve Banks pursuant to such a refunding would not be subject to the $5 billion limit stated in section 14(b) of the Federal Reserve Act and that, subject, of course, to usual questions regarding monetary and credit policy and the terms eventually set for the refunding security, the Federal Reserve Banks would be prepared to consider refunding some or all of their maturing securities under such a proposal.
>
> The Committee has reviewed the proposal in your letter of April 13, 1960, as modified by your oral statement referred to above, and has concluded that, like the arrangements proposed in October of 1958, acquisitions by the Federal Reserve Banks pursuant to such a refunding would not be subject to the $5 billion limit stated in section 14(b) of the Federal Reserve Act. Furthermore, since it is contemplated that a substantial group of other investors would be eligible to refund on the same basis as the Federal Reserve Banks, the objection to the first proposal made in 1958 would not seem to apply. (It is assumed that the circular would contain an appropriate statement regarding the subscriptions to be allotted in full.) Accordingly, subject to usual questions regarding monetary and credit policy and the terms eventually set for the refunding security, the Federal Reserve Banks would be prepared to consider refunding some or all of their maturing securities under such a proposal.

It was agreed that the next meeting of the Federal Open Market Committee would be held on Tuesday, May 24, 1960.

At the request of the Chairman, Mr. Young commented on developments in connection with the statistical program on the Government securities market. He reported that the program was moving ahead satisfactorily in terms of the planning of schedules and relations with the dealers, and it was intended to request the dealers to begin reporting on May 20, 1960. However, one problem had arisen. One dealer (Aubrey G. Lanston and Co.)

had raised questions about the access of the Desk to the individual dealer reports that were to be submitted to the newly-organized Market Statistics Department of the New York Reserve Bank. These questions having been raised, it seemed desirable to advise the dealer candidly as to the pertinent provisions of the plan. Therefore, it was stated that the individual dealer reports would not usually be available to the Desk, but that (1) in the extension of repurchase agreements the Desk could call for and obtain from the Market Statistics Department certain figures that would be helpful from the standpoint of the extension of credit, (2) in the event of the declaration of a disorderly market the Manager of the Account would have full access to individual dealer reports until the situation was corrected, (3) to provide against contingencies the Desk could seek permission from the President of the Federal Reserve Bank of New York to have access to dealer reports, and such permission could be granted in certain circumstances. A fourth provision of the plan, namely, that the Treasury might request compilations of individual dealer reports that would be helpful in appraising underwriting experience over a past period, had not been mentioned to the dealer because that provision was not pertinent to his inquiry.

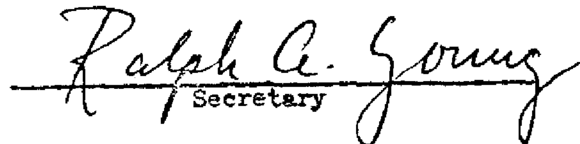
Mr. Young went on to say that the dealer later expressed the view that by and large the statistical program was good and that the firm would be glad to cooperate, but that in view of the provision for access of the Desk to dealer reports in the event of contingencies the dealer had reservations and, unless something was done in that respect, would have

to decline to participate in the program. However, the dealer suggested exploration of a possible compromise with those concerned, namely, that this dealer and other dealers would be informed promptly on each occasion in which contingency access was granted. If such assurance were given, the dealer indicated that his firm would go along with the program. Mr. Young added that the Treasury and the New York Reserve Bank had been kept informed of developments.

It was indicated that efforts would be continued to work out a solution to the problem that Mr. Young had described.

The Chairman then referred to comments at the April 12 Committee meeting regarding the likelihood of heerings by a Subcommittee of the House Banking and Currency Committee on one of several bills pertaining to the Federal Reserve System that had been introduced by Congressman Patman, and to the subsequent development, reported to the Reserve Bank Presidents, concerning a change of plans under which the Subcommittee had indicated that the hearings would relate to a different bill, (H. R. 8516), also introduced by Mr. Patman. The Chairman stated that the Presidents would be kept advised as additional information regarding the hearings became available.

The meeting then adjourned.



Secretary