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 24, 1960, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Hayes, Vice Chairman
Mr. Balderston
Mr. Bopp
Mr. Fulton
Mr. King
Mr. Leedy
Mr. Mills
Mr. Robertson
Mr. Shepardson
Mr. Irons, Alternate for Mr. Bryan

Messrs. Leach, Allen, 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, Hostetler, 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
Mr. Patterson, First Vice President, Federal Reserve Bank of Atlanta
Mr. Daane, Vice President, Federal Reserve Bank of Minneapolis

Messrs. Willis and Anderson, Economic Advisers of the Federal Reserve Banks of Boston and Philadelphia, respectively
Mr. Coldwell, Director of Research, Federal Reserve Bank of Dallas
Messrs. Black, Netzer, and Lynn, Assistant Vice Presidents of the Federal Reserve Banks of Richmond, Chicago, and San Francisco, respectively
Mr. Holmes, Manager, Securities Department, Federal Reserve Bank of New York
Mr. Bowsher, Economist, Federal Reserve Bank of St. Louis

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the Federal Open Market Committee held on May 3, 1960, were approved.

At the meeting of the Committee on May 3, 1960, Mr. Young reported on questions that had been raised by Aubrey G. Lanston and Company, Inc., regarding that firm's participation in the Treasury-Federal Reserve program of Government security market statistics. Thereafter, with the concurrence of the available members of the Committee, as indicated by advices transmitted to the Secretary upon distribution of a draft, the following letter was sent to the President of Lanston and Company on May 17, 1960, over the signature of President Hayes of the Federal Reserve Bank of New York:

"This is in reply to your letter of May 10 addressed to Miss Madeline McWhinney and relating to the Treasury-Federal Reserve program of Government security market statistics. Your letter raised two points of procedure regarding the handling of reports of dealers to this Bank.

"Concerning the first point, the major objective of the new Treasury-Federal Reserve program has been to develop data on the Government securities market appropriate for public information. We recognize, however, that prior to launching a

"continuing release of such statistics, some experience in the processing and interpretation of such data is necessary. Therefore, as explained in earlier meetings between our staff and members of your firm, we have planned an experimental period of data collection of several months duration, during which no statistics would be made public. Following this period of familiarization, we further plan to contact the dealers again regarding problems of publication. At that time we will solicit suggestions from each dealer on the content and form of series to be released as well as seek dealer views on the time lag between collection and release date. We have never proposed, however, to make our publication program in this area dependent on the individual approval of specific dealers as to the details of the aggregate data to be released.

"Concerning your second procedural point relating to the exceptional conditions under which individual firm data will be available to persons outside the Market Statistics Department, I understand that Mr. Ralph A. Young of the Board's staff has already talked to Mr. Youngdahl at some length about the explicit procedures that the Treasury and Federal Open Market Committee have adopted in order to limit access to individual firm data to specially authorized occasions and persons. As Mr. Young indicated, with the exception of the few summary figures that may be requested by the Manager of the System Open Market Account for individual dealers seeking repurchase accommodations at this Bank, availability of individual firm data outside the Market Statistics Department under special conditions is expected to be rare.

"To illustrate specifically the type of conditions under which such exceptional release of data could occur, I can perhaps be most helpful by listing the situations presented for the consideration of the Federal Open Market Committee at the time it authorized the new market statistics program:

"1. The Manager of the Open Market Account may have full access to individual dealer reports in a market situation determined to be disorderly.

"2. In other circumstances of an exceptional nature, the Market Statistics Department might be directed by the President of the New York Federal Reserve Bank to make selected or full details of individual dealer reports available to qualified System officials designated for examination and study.

"3. In connection with any Treasury financing, the Treasury might, on occasion, request the President of the Federal Reserve Bank of New York to direct that special data be supplied as to individual dealer holdings of issues specifically involved in, or closely related to, the financing in question.

"It is impossible for us to foresee at this time how many special occasions for access to individual dealer reports might arise. If any respondent in the program would wish to raise the question after several months of experience, we foresee no reason at this time why an answer might not then be supplied. All instances of access to individual dealer figures will be reported to the Federal Open Market Committee and to the Treasury so that an official record will be maintained.

"I am, naturally, pleased to be informed of your preparations to cooperate in our program. The expectation of the Treasury and the Federal Open Market Committee is, of course, that all of the dealers will respond cooperatively to our joint request for the statistical material needed to fulfill the program that both agencies are undertaking jointly, through the Federal Reserve Bank of New York, in the public interest. In closing, may I assure you that the handling, the processing, and any exceptional official assess to individual dealer figures will be protected at all times by the strictest standards of confidentiality. The program will receive careful staff review from time to time and substantive or procedural change believed to be desirable may be recommended in the light of such reviews.

"Since these matters are of interest to all reporting dealers, we are passing the substance of this letter along to other dealers without mentioning your firm or referring specifically to the questions which you raised."

The action taken in sending the foregoing letter was ratified by unanimous vote.

In this connection, Mr. Hayes commented that the Lanston firm had subsequently informed the New York Reserve Bank that it would cooperate in the statistical program. Thus, all of the Government securities dealers were participating.

Before this meeting there had been distributed to the members of the Committee a report of open market operations covering the period May 3 through May 18, 1960, and a supplementary report covering the period May 19 through May 23, 1960. Copies of both reports have been placed in the files of the Committee.

Mr. Rouse made the following comments with respect to developments since the meeting on May 3, 1960:

As the written report to the Committee points out, the statistical reserve position of member banks, whether measured by total reserves or by net borrowed reserves, has been on average somewhat easier than it had been in the preceding interval between Committee meetings. The money market, on the other hand, did not reflect this statistically easier position, and Federal funds traded almost consistently at the 4 per cent ceiling. The reasons for this divergence are not wholly clear, but it appears that they center on unusually large movements through Treasury Tax and Loan accounts in both the past and the preceding period, which affected temporarily the distribution of funds between the money market banks and the country banks. There were large calls on all banks and subsequent heavy redeposits in "C" banks which were in turn recalled.

Treasury bill rates fluctuated widely again over the past three weeks. In the auction on May 16 the three- and six-month Treasury bill rates were established at 3.79 and 4.00 per cent, 1/2 per cent higher than in the previous auction. Bill rates moved sharply downward last Thursday and Friday to about 3-1/8 per cent and 3-1/2 per cent on the three- and six-month bills, respectively, but bounced back to 3-1/2 and 3-7/8 per cent in the auction yesterday. The relative instability of our short-term rate structure has been a source of increasing perplexity, and concern, to many bankers here and abroad, and it is a phenomenon to which the Committee may have to pay increasing attention. Basically it reflects the fact that the market has become dominated by the nonbanks, and the bill rate has, as a result, become increasingly divorced from the reserve positions of the banks. Rate movements in the past period, however, were in part a reflection of the tense international situation and of the sour reception by the market of the Treasury's announcement that it would add $100 million to the six-month bill issue in the May 16 auction. While adding to the bill offering has always been considered a rather routine way of raising relatively small amounts of cash, the dealers felt, in this case, that the Treasury was undermining their positions at a time when they were in the process of distributing the new certificates and notes offered in the May refunding operation.

The Treasury has no urgent need for additional cash at the present time, but would like to build up its cash balance so that it can enter into the next financing period, early in July, in a stronger position than it did in April. This would indeed be a desirable development from the System's point of view, since it

would undoubtedly make the task of maintaining an even keel during Treasury financing operations easier to accomplish. It now appears that the Treasury believes it can get by with a $3 billion cash financing in early July and at the same time pay off $0.5 billion of the special July 15, 1960, bills on maturity. This would mean that the Treasury would offer only $1-1/2 billion one-year bills in July. I should also report that with June free from normal financing operations, the Treasury is giving serious thought to whether it should attempt a partial advance refunding of the $11 billion 2-1/2's of 1961. Developments in the international situation probably hold the key to the Treasury decision, although there are a number of technical problems to be resolved. As you know, the legislative authority for the System to lend directly to the Treasury up to $5 billion outstanding at any one time expires next June 30. Under Secretary Baird advises us that the Treasury has requested the Congress to renew this authority.

System operations in July 15 Treasury bills are fully detailed in the memorandum prepared by Mr. Larkin, and mailed to you last Friday. So far, $91.5 million July 15 bills have been purchased under the authorization made by the Committee on April 12, of which $48 million were on a swap basis. This brings total System holdings of July 15 bills to $104.9 million.

I should also like to call your attention to a slight change in the regular written reports to the Committee. In view of the growing interest within this group in various measurements of bank reserve positions, we have added data on total reserves, borrowings, and nonborrowed reserves to the table describing the factors affecting bank reserve positions, and their inclusion will be continued in subsequent reports.

Thereupon, upon motion duly made and seconded, and by unanimous vote, the open market transactions during the period May 3 through May 23, 1960, were approved, ratified, and confirmed.

Supplementing the staff memorandum distributed under date of May 20, 1960, Mr. Noyes made the following statement with regard to economic developments:

A large volume and variety of economic information has become available since the last meeting. At that time the impression that April would show considerable improvement over the curtailed levels of March was based on a few weekly series, some informal reports by businessmen, and an obvious change in the weather.

Most of the additional information we have supports the earlier view. Certainly, retail trade improved substantially and the improvement was general--extending to both durables and nondurables. Employment increased, and unemployment declined more than seasonally. With prices of farm and food products back up to year-ago levels from their low point of last fall, and crop prospects generally excellent, farm income should improve as the year progresses.

One way to summarize the widespread nature of the shifts from March to April is in terms of diffusion indexes for leading and coincident indicators, virtually all of which increased in April. On a month-to-month basis, a diffusion index for five groups of leading series was above 50 per cent in April, after hovering in the low 30's in February and March. Similarly, the index for the three roughly coincident groups was up above 70 per cent, from the 40's in the preceding months.

The question, of course, is whether this rather dramatic improvement from March to April is significant, or whether it was due to transitory factors influencing each of these months in opposite directions. The scattered information we have so far for May suggests that the latter may well be the case. Department store sales have certainly reacted from the very high levels of last month. More important, perhaps, the steel rate has continued to drop off as new orders for steel are running considerably below current production. In fact, new orders in durable goods manufacturing generally were off somewhat further in April. With this weakness in the basic industries, there is little chance that the index of industrial production will increase in May, and it will take unusual strength in the nondurable sector to even hold the March-April level. Thus, the average physical output at factories and mines in the second quarter will almost certainly be below the first quarter.

If consumption expenditures are maintained at the rates indicated for April and May, there is a good chance that the gross national product in the current quarter will not show a decline, and perhaps a small increase. However, the advance from the same quarter of 1959--a growth of only about 4 per cent or less--will be disappointing for a period in which more vigorous expansion was widely anticipated on cyclical grounds.

In what I have said thus far, I have abstracted from the economic repercussions of the failure of the Summit Conference. Broadly speaking, these repercussions might be of two types. First, they might be reflected in a changed attitude on the part of businessmen and consumers--a renewal of inflationary expectations, accompanied by an acceleration of durable goods purchases, a higher rate of inventory accumulation, and all of the other actions that are provoked by fear of rising prices, or perhaps even physical shortages. Washington is a singularly

unsuitable vantage point from which to judge whether such a psychological reaction has, in fact, occurred; but no evidence of it is apparent.

The second area in which the repercussions of the Summit failure might appear is in the expenditures of the Government itself. It has been suggested by a number of observers that intensification of the cold war, which now appears almost inevitable, will lead to an increase in Federal spending and a less favorable fiscal position than was suggested by the budget for 1961. At least in the first instance, such increased expenditures would be likely to appear in the appropriations for the defense establishment, for military assistance, or both.

We had undertaken an analysis of recent and prospective defense expenditures prior to the scheduled Summit Conference, in the hope that it might shed some light on the erratic behavior of the economy so far this year, and for that reason we have assembled somewhat more detailed information on current and prospective outlays in this area than would normally be the case.

This information would appear to support the official position taken in recent statements by the Secretary of Defense and his Deputy that the outcome of the Summit Conference should not have an appreciable effect on defense spending.

New orders placed by the Defense Department are scheduled to increase considerably in the second quarter, but this is in line with a well-established seasonal pattern of defense ordering and had probably been anticipated by most suppliers.

The defense budget for 1961 already involves a substantial further shift from manned aircraft to missiles, and provides for procurement of those missiles which are expected to become operational at rates which constitute the practical capacity for their production in 1960 and 1961. Hence, there would be little immediate advantage to be gained from increased appropriations for missile procurement. In this connection, it should be remembered that while the space program has encountered special difficulties and disappointments, the military missile program is proceeding roughly according to schedule, and witnesses for the defense establishment have all testified that it is not being substantially retarded by lack of current appropriations. Defense expenditures for fiscal 1959, fiscal 1960, and the budget for 1961 are all close to an annual rate of $41 billion. Thus, in the absence of a general reorientation of the defense program, it appears that military expenditures in the period ahead are not likely to be a positive force in general economic developments. In one sense defense procurement may be a depressing factor as the further shift toward more missiles and prototype bomber

development, rather than current procurement, will accentuate a trend that has been going on since 1957, in which each dollar of defense procurement has represented a smaller and smaller amount of man-hour employment and conventional resource utilization. Unless there is a widespread shift in attitudes and expectations, or the stimulus of increased military procurement, the prospect appears to be that we will see operations in many basic industries for a period at rates well below capacity levels, and more unemployment than has been associated with high-level activity in previous postwar periods.

There are always uncertainties as to the future, and these are most pronounced when the economy is showing no signs of decisive movement in one direction or the other, but, as I have tried to bring out in earlier reports, as time passes without any unequivocal evidence of an upward thrust and accompanying inflationary pressure, the chances that such a development will occur are substantially diminished and the need for a restrictive monetary policy is correspondingly lessened.

Mr. Thomas presented the following statement with respect to financial developments:

Recent credit developments indicate that neither borrowers nor lenders have responded with any alacrity to the increased availability of bank reserves. Although interest rates continue below the peaks of last winter, they tend to fluctuate widely in reflection of any actual or anticipated variations in supply or demand conditions.

The upturn in total bank credit that occurred in April, as banks underwrite the Treasury financing, has been followed by a decline in total loans and investments at city banks in the first three weeks of May. Holdings of Government and of other securities were reduced and loans on securities also declined, while loans to businesses, finance companies, and consumers increased moderately. New capital issues have continued at a moderate level, and mortgage lending is no doubt below last year's peak volume. The increase in the money supply, seasonally adjusted, that seemed to be occurring in late March and early April has not continued. U.S. Government deposits at banks, however, have risen much more than was expected.

Estimates of flows of funds, that can now be made on a preliminary basis for the first quarter of this year, indicate the changed nature of credit demands compared with last year. The net increase in all credit and equity market instruments, which

attained a record volume in 1959 as a whole, was substantially smaller in the first quarter of 1960 than in the same period last year but comparable with the corresponding 1958 quarter. The most striking change, of course, was the shift of the Federal Government to a position of debt reduction by an amount that may be considered as normal for the first quarter of the year. In addition, the increase in aggregate private credit was a little less than a year ago. Businesses borrowed somewhat more, accounted for by an increase in bank loans. Consumer indebtedness, however, increased less than in the first quarter of last year, reflecting principally a lower volume of mortgage loans. Partial data indicate that similar contrasts with last year have characterized the second quarter.

With respect to sources of funds, gross saving by consumers in the first quarter of 1960 was slightly above last year's high volume, while saving by nonfinancial business was somewhat smaller. Consumers invested more of their savings in tangible capital expenditures, including durable goods, and also borrowed less than they did last year. Thus the volume of funds available for acquisition of financial assets was reduced. Most of this reduction occurred in holdings of deposit-type assets--demand deposits declined more than last year and savings deposits and shares increased less. Individuals' purchases of Government securities were smaller than a year ago--though still substantial--while purchases of other securities and mortgages were larger.

Nonbank financial institutions, receiving smaller amounts from consumers, also advanced less credit than they did last year. Credit supplied by the commercial banking system showed a much larger decline in the first quarter of this year than usual, corresponding to the greater than seasonal decrease in deposits. In essence, these data point up the market contrast between this year's credit situation and that of a year ago, brought about principally by the shift in the fiscal position of the Federal Government. Yet, it also is significant that other credit demands have not increased so as to offset the decline in Government borrowing. Saving has continued at a high level, but more savings have gone into tangible assets and there has been a lessened flow of funds into credit and equity markets. As a net result there has been a lessening of pressures toward rising interest rates.

Interest rates have declined from the peak levels reached in the latter part of 1959 and in early January of this year, but they are still higher than they were in the first four or five months of 1959. In view of the moderation in aggregate credit demands, which persisted since early this year, question may be

raised as to why interest rates are not lower. What has kept them from returning to earlier levels? One possible explanation is that something like the current level of interest rates is necessary to attract savings into financial assets. Another is that the shift by the public from bank deposits to other financial assets has resulted in increasing the pressures on markets for short-term securities to meet current cash needs. These varying pressures can surely account for some of the wide fluctuations that have recently been characteristic of Treasury bill rates.

A third possible explanation, and one deserving particular attention by Federal Reserve officials, is the impact of System policies. To be sure, positive measures have been taken to ease restraints on the availability of bank reserves. Yet, as mentioned earlier, the response has not been notable. It may be that the demand factors are not sufficiently vigorous and could not be stimulated by more abundant credit availability or lower interest rates. In such an event interest rates should decline. It may be that banks still feel restrained and are holding back rather than pushing credit extensions. Possible reasons for this attitude deserve scrutiny.

One is that, while bank reserve positions are easier than they were during the latter half of 1959, they are not any easier than they were in late 1958 and early 1959 or in early 1955 and late 1956--all periods of expanding credit demands but of lower interest rates than at present. Member bank borrowings at the Reserve Banks of over half a billion dollars tend to be restrictive unless credit demands are very vigorous. Last year's policies of heavy Treasury borrowing, partly underwritten by banks, followed by bank liquidation of Government securities to obtain funds for loans was a process that made possible credit expansion under restraint.

In addition, banks have been borrowing large amounts from others. Such borrowings recently have generally exceeded $2 billion. Their possible impact deserves some study. It has commonly been considered that since the bulk of these borrowings are within the banking system and consist largely of Federal funds transactions, the restraint on borrowing banks is counterbalanced by the effect of liquid funds available to the lending banks.

Our newly developed figures on Federal funds transactions, however, indicate that some of the borrowing by banks is not from other banks and is not all Federal funds. The new figures from dealers in Government securities, available for only one or two days, suggest that these dealers may be important intermediaries

between banks as borrowers and corporations and others as lenders. Dealers' "reverse repurchase agreements" with banks exceeded their borrowings from banks. The bulk of dealer financing was obtained from corporations. These data, of course, need a longer period of study before definitive conclusions can be drawn as to their significance.

Another likely factor of restraint on banks at present is the level of the Reserve Banks' discount rate relative to market rates. This may be more of a restrictive factor than the volume of borrowings and undoubtedly accounts for some of the wide fluctuations in Treasury bill rates. This is the case not only because banks owning bills and needing reserves prefer to sell bills at the market rates prevailing than to borrow at the higher discount rate. It is also true because banks--and others--possessing available funds that they want to keep in liquid form can sell Federal funds, i.e., lend the funds to other banks or to dealers, at a higher yield than they can obtain from the purchase of Treasury bills. Banks purchasing the funds thus avoid borrowing from the Reserve Banks. Such borrowing would have had the effect of supplying additional reserves to the market. It might have induced additional Federal Reserve purchases of securities to relieve the strain. The additional reserves would have been conducive to further bank credit expansion.

Recent behavior of the money market supports the view that the maintenance of the discount rate above market rates is an effective penalty on borrowing and credit expansion. The question to be considered at present is whether it is exerting more restraint than is desirable under the circumstances. The review of credit developments to date indicates that this may be the case. There are few, if any, indications of excessive uses of credit that need to be restrained--unless it be in the area of consumer instalment credit. Whether the dramatic events in the international political area will change this picture raises serious questions that at this stage are matters of conjecture and judgment. They need to be considered, nevertheless, before taking any overt action that would be interpreted as a shift of policy.

As for the period immediately ahead, seasonal demands will exert a substantial drain on reserves during the next two or three weeks. This drain will equal $400 million or more, and at least half of that amount will continue to be needed through the last half of June, when markets will be under the pressure of seasonal liquidity needs. Substantial additional amounts will be needed early in July to meet holiday currency demands. After mid-July, seasonal reserve needs will not increase further until the Labor Day week end.

If it seems appropriate to encourage a resumption of bank credit growth, $400 million or more of additional reserves might be supplied in the course of the next three to six weeks. A reduction in the discount rate might accomplish the same purpose with a somewhat smaller volume of open market purchases.

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

No new data have become available since the last meeting of this Committee which would change significantly the picture, justifying an attitude of relative optimism with respect to recent developments in our balance of payments, that I have been presenting at recent meetings of the Committee. I would like, of course, to stress very strongly that the optimism that would seem to be justified is in fact only a very relative optimism: relative, that is to say, to some of the extremely pessimistic views as to our balance-of-payments prospects that one still hears expressed. Certainly it would not do, for example, to put any particular stress upon the fact that gold purchases by foreigners (which, in the first quarter of this year, as I reported a couple of meetings back, were, at $42 million, less than half the already relatively low figure for the first quarter of last year) were almost negligible in the first three weeks of May. (Actually, including a transaction announced but not yet executed, the total of gold sales to foreigners in those three weeks was below $5 million.) One should not overstress such figures, in the first place, because gold movements are very erratic in the short period. In the second place, even over a longer period--although this is still a hard thing for many people to understand --gold movements are not necessarily a good indicator of what is happening to the balance of payments; and it is the balance of payments which must remain our primary source of concern.

From this standpoint, there is one matter which does seem to me to deserve further comment. In my reports to this Committee, in undertaking to account for the international movements of gold and dollars, which we do take as a measure of what has been happening to our over-all balance of payments, I have concentrated on what the trade figures--the figures for exports and imports--have been showing. This has been quite deliberate: for the simple reason that, in the long view, it is our performance in the field of commodity trade that will decide whether our international accounts are or are not going to be balanced at a

high level without the imposition of arbitrary restrictions. But this is not to say that we can leave the so-called "invisible" items in our balance of payments altogether out of account; and this is especially true with respect to the particular "invisible" item which is represented by the movements of capital. More specifically, one should ask: are the capital items in our balance of payments currently moving in our favor or are they currently moving against us?

The answer, so far as the figures for the first quarter of this year are concerned (and these are the latest figures available to us) is, quite clearly, that the capital items on balance moved against us during that quarter of this year, to an extent of the general order of magnitude of $200 million, as compared with the first quarter of 1959. If the noncapital items in our balance of payments had remained the same, this would have meant, of course, that gold and dollar transfers to foreigners would have been higher by that amount than they were a year ago. Actually, however, gold and dollar transfers to foreigners in the first quarter of 1960 were about one-fourth less than they were a year ago. From this set of facts, some obvious conclusions can be drawn:

First, it is clearly wrong to suppose, as so much of recent discussion seems to have been supposing, that we can come to a conclusion as to what is going to happen to the size of our balance-of-payments deficit solely on the basis of what may be happening to the capital movements component in the balance of payments. Specifically: a very considerable part of the discussion to which I have referred has rested on the assumption that if, as the result of a differential interest-rate structure here and abroad, capital--particularly short-term capital--moves out, we shall find ourselves losing "gold," and therefore are likely to find ourselves effectively barred from any efforts that we might otherwise have wished to make in the direction of a countercyclical monetary policy.

I do not enter here into all the weaknesses of this argument: for example, its great exaggeration, by implication, of the proportion of foreign balances held in the United States which can be said to be "interest-sensitive" in the degree which the argument suggests; or its ignoring of the difference between a country such as the United States, which still hold relatively massive reserves in relation to its foreign obligations, and a country such as the United Kingdom, whose reserve position is much more tenuous. My point is simply that it is wrong to talk about the future of our balance of payments as if it depended solely, or even primarily, on capital movements (and short-term

capital movements, at that) without regard to what is happening to the central matter of trade--the basic relation between our exports and imports of commodities. I have tried to illustrate the point particularly by the experience of our balance of payments thus far this year as compared with the experience last year. This year, I have pointed out, despite a shift against us in capital movements, our balance of payments deficit this year is significantly less than it was at this time last year because the improvement in our trade position has been much more than enough to offset the adverse capital movements.

This in itself is, I think, an encouraging finding, precisely because it is in the field of trade, and all that "trade" implies in the way of technical efficiency in production and competitiveness in the broadest sense of the term, that the adjustments required in order to bring our international accounts into close balance are the most difficult to make: much more difficult, for example, than is implied by the suggestion that the balance can be brought about simply by keeping our interest rate structure higher than that of our trading partners at all times. Monetary policy certainly has a critical role to play in the process of adjustment of our international accounts; in my own view it has already played a role in that process which is certainly not to its discredit. What is to be rejected is not the conception of a role for monetary policy in the process of balance-of-payments adjustment, but a conception of it, in relation to differential interest-rate structures and short-term capital flows, which rests on so narrow a technical base that it misses the really essential point even within the field of capital movements: namely, that capital moves internationally not only in response to interest-rate differentials, but also on the basis of a judgment by the well-informed as to whether the monetary authorities of the countries in question have an adequate understanding of their responsibilities, in relation to the twin goals of containing inflation and fostering sustainable growth, and adequate courage and determination to carry the fruits of that understanding into accomplishment.

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

On the whole, statistical data of the last three weeks lend considerable support to the views already held by a good many in the System, including my associates in New York, to the effect that further moderate expansion in business activity

this year is a reasonable expectation--but with no likelihood of a real surge involving inflationary pressures. The basic outlook has remained about the same through a disappointing March and an encouraging April. Naturally the sudden worsening of the international situation could have major effects on the domestic economy, but neither the extent nor even the direction of such effects is yet visible. Of course we must expect a sharp decline in the rate of total inventory accumulation in the second quarter. However, this may be offset by gains in final consumption. Favorable factors include continuing optimism on the part of consumers and businessmen, although this is tempered, in the case of businessmen, by rather sober profit expectations for the remainder of the year, attributable in large part to increasing price competition. Housing starts reported for April, and for March on a revised basis, suggest that residential construction may have bottomed out. While steel output has continued to drop, there seems to be substantial evidence that inventories are being drawn down, which should limit further declines, especially with plant and equipment spending on the rise.

Although unemployment is clearly higher than it should be, the problem seems to be due in large part to inadequate training and inadequate mobility of labor--causes which are not easily influenced by credit availability.

Demand for credit is generally strong but not excessive. Total loans and investments of all commercial banks rose sharply in April, reflecting a roughly seasonal expansion of business loans, unusual strength in other loan categories combined, and a large increase in holdings of Government securities incident to the April Treasury financing. Loan demand has been less insistent in New York than elsewhere, but this seems in line with the usual seasonal pattern. The money supply still shows a drop of about one-half per cent in the past year. On the other hand, the Board staff's new statistics on total liquid assets held by the nonbank public emphasize the sharp contrast between liquidity as measured by this total and liquidity as indicated by the money supply alone. In the first quarter, for example, liquid assets rose at an annual rate of 3-1/2 per cent, while the money supply fell at an annual rate of 2 per cent. It is interesting to note that in the past nine years the year-to-year increases in liquid asset holdings have been both much steadier and considerably larger, on the average, than the increases in the money supply.

The corporate bond market has been quite steady, although the calendar of new issues scheduled for the next thirty days is higher than at any time in 1959 and 1960.

It seems to me that the satisfactory business outlook warrants maintenance of our recent policy which might be characterized as one of substantially lessened restraint as compared with a few months ago. It does not, in my judgment, call for any further easing action at this time. Another consideration suggesting a steady policy is the uncertain economic and political impact of recent international developments. Moreover, an even keel policy will be appropriate if the Treasury undertakes an advance refunding program in the next few weeks.

I should think that the Manager might be instructed to pursue the same open market policy as in the past three weeks, with emphasis on the feel of the market rather than any specific target. The projections clearly indicate that substantial outright purchases and/or repurchase agreements will be required in the next three weeks. Liquidation of bills by corporations and others prior to the June 15 tax date, and perhaps some preliminary window dressing, should supply bills to the market, and this may minimize the impact of System purchases on market rates of interest.

As for the discount rate, I recognize that a case might be made for a reduction at this time on the grounds that the 4 per cent rate was adopted last September at a time when inflationary expectations were far stronger than now; that there is some question whether current business conditions justify the highest discount rate of the last 30 years; that with business still rather strong we could reduce the rate without the danger of signalling fear of recession on the part of the Federal Reserve; and that a lower rate would put us in a better position to increase it at some later date when firmer restraint might be needed.

However, in my judgment there are even stronger reasons for taking no action on the discount rate. As we look back a few months, I think we can conclude that the existence of the 4 per cent rate since last September has had a good stabilizing influence; and we can certainly be glad that we resisted the temptation to increase it in January when temporary market pressures pointed strongly in that direction. Later the 4 per cent rate probably helped deter market rates from dropping even lower than they did. At present neither business nor credit conditions call for any overt signal--and the gap between the discount rate and market rates, which is not excessive in any case and is not creating any problems of discount administration, may tend to narrow as seasonal pressures on market rates increase in the next couple of months--including the influence

of the Treasury's prospective shift from surplus to seasonal deficit. Moreover, the credit markets appear to be pretty well stabilized, suggesting that it might be best not to "rock the boat."

Having just returned from Europe, I can't help giving some weight to the consideration that any reduction in our discount rate could tend to accentuate the flow of short-term capital to Europe--a flow which is already raising difficult problems for some of the European central banks. Also, as I have already mentioned, the post-Summit uncertainty of international affairs in general would point to the wisdom of deferring any change in credit policy, even if a change were indicated by domestic considerations--and in my judgment it is not indicated on that score. So I come out with a clear conviction that we should leave the rate unchanged between now and our next meeting.

With respect to the directive, I would still like to see a procedural change in the way of separating long-range goals from immediate objectives--but there is no urgent need for such a move immediately.

Mr. Erickson said that business performance and sentiment in the First District had improved somewhat, and that business reports were generally good. The New England production index was up in February and remained at the same level in March. There was nothing new to report on construction or employment. In recent weeks, total claims for unemployment compensation and additional claims had been running higher than a year ago, but the rates were not as high as nationally. Retail sales were ahead of last year, and new automobile registrations were ahead by 30 per cent, a rate of gain higher than the national average. The April survey of mutual savings banks showed an increase in deposits of 4.6 per cent, slightly less than in other recent months. During the past three weeks purchases and sales of Federal funds by reporting banks were about in balance, but there was slightly greater use of the discount window, with more banks coming to the window than in the preceding three-week period.

Mr. Erickson said that he would not recommend a change in the discount rate or the directive at this time, although he did not feel too strongly about the directive. With the System having been supplying reserves, he was rather surprised that the Federal funds rate did not go below 4 per cent, except for a day or two, during the past three weeks. As to open market operations in the forthcoming period, he would favor giving the Desk the same instruction as at the meeting of the Committee three weeks ago. He would supply needed reserves freely, and he hoped there might be a number of days when the Federal funds rate would not be at the discount rate.

Mr. Erickson commented that he would like to see a paper prepared on interest rates that would review the past two or three years, particularly in light of factors such as the increased use of Federal funds, the greater use of short-term securities, including Treasury bills, by nonbank interests, and the fact that the Treasury was unable to undertake long-term financing at rates in excess of 4-1/4 per cent.

Mr. Irons reported mixed movements in the Eleventh District, with economic activity at a generally satisfactory over-all level. Department store sales thus far in May were off somewhat from a year ago, while the oil situation was unchanged and apparently would be substantially unchanged for some time. There had been a slight decline in construction, but employment was satisfactory and the agricultural outlook was quite good.

With regard to the banking situation, Mr. Irons said that in the past three weeks District banks lost deposits and loans and investments declined somewhat. Bankers in the larger cities with whom he had talked recently reported a strong demand for credit and stated that they were being selective in granting applications for loans. They indicated that if more funds were available, they would be making more loans. Borrowing at the Reserve Bank had increased in terms of the number of banks borrowing, with more of the larger country banks coming to the window. The large city banks continued to operate substantially in the Federal funds market; during the past three weeks purchases of Federal funds had been running around $450-$475 million, with sales around $150 million. Had it not been for the use of Federal funds, more banks would have been coming to the discount window.

With respect to Federal Reserve policy, Mr. Irons said that although he had not been dissatisfied with open market operations during the past three weeks, he was concerned and confused by the fact that the lessening of restraint over a period of some six weeks appeared only to have reflected itself to any degree in New York City. Upon reviewing statistics on reserves and borrowing since the first of April, it appeared to him that on average reserve city banks showed substantial net borrowed reserves of around $200-$250 million. On the other hand, New York City banks had not been borrowing from the Federal Reserve and free reserves

had appeared quite frequently. The Chicago picture seemed to be more like that of the reserve city banks. Thus, it appeared that the results of the lessening of restraint were not extending to a substantial part of the banking system, that is, the reserve city banks. If the System really wanted to lessen restraint and encourage an increase in the money supply, it occurred to him that this might be a situation in which it would be desirable to make a further change in the amount of vault cash permitted to be included in required reserves, with the adjustment of such a nature as to allow the reserve city banks to reap some benefit. In suggesting this, he was not arguing for a lot of ease, but the statistics appeared to bear out his feeling that what the System had been trying to achieve was not flowing through to a substantial part of the banking system. A further release of vault cash might be a way to supply a reasonable amount of additional reserves and distribute them widely. The action could be defended on the basis of seasonal demands as well as a desire to encourage an increase in the money supply. Thus, while he was not sure whether he would favor this procedure, there seemed to be some basis for it.

Mr. Irons went on to say that he would prefer to leave the discount rate unchanged at this time, his position being in accord with that of Mr. Hayes. In considering any reduction of the discount rate, the Federal Reserve would have to decide whether it wanted a general lessening of restraint over the entire banking system or whether it wanted

to aid special cases. He would prefer to keep the present discount rate until there was evidence of some adjustment of market rates. One reason why the Federal funds rate had not drifted away from the discount rate appeared to be that, on the one hand, the Reserve Banks were trying to administer the window in accordance with the principles of Regulation A pertaining to continuous borrowing while, on the other, member banks were in need of funds. In conclusion, Mr. Irons said he was not particularly concerned about the policy directive.

Mr. Mangels summarized the results of a poll among members of the California Bankers Association which showed that 58 per cent of the respondents expected business to continue at present levels during the second half of this year, while 26 per cent expected an upturn and 16 per cent a decline. Some 78 per cent felt that inflation had not been checked, while 82 per cent thought that interest rates would remain fairly steady for the remainder of the year and only 2 per cent foresaw an increase.

Turning to the Twelfth District economy, Mr. Mangels said there had been no outstanding changes recently, although conditions probably were slightly better than a month ago. In April, unemployment was at 4.2 per cent, against 4.5 per cent in March. About half of a gain of .3 per cent in employment in April was accounted for by the employment of persons in connection with the taking of the census. Steel production in May was holding at about the April level of 71 per cent of capacity, but it was

felt that production probably would drop further in the next month or two. Lumber production again declined, and in late April and early May some mills in the Pacific Northwest had closed temporarily because of the weakness of demand. Department store sales during the four weeks ended May 14 showed no change from a year ago. In the first quarter of this year, farm cash receipts were 5 per cent higher than in the corresponding period of 1959.

With respect to the banking situation, Mr. Mangels reported that during the three weeks ended May 11 loans were down $50 million, holdings of Government securities were down $188 million, and demand deposits were down $579 million. Time deposits were up $87 million and savings deposits were up $32 million, most of the increase occurring outside of the State of California. Borrowings from the Reserve Bank were quite nominal. Trading in Federal funds was quite active, with purchases and sales about in balance.

Mr. Mangels noted that while there had been some slight improvement in business conditions, over all, no upward push was evident and there seemed to be rather general concern about the future. Under these conditions, he felt that the Committee would be justified in continuing its policy of easing. He would look forward to a zero balance in net borrowed reserves, with perhaps even a period of a week or so when there would be free reserves.

As to the discount rate, Mr. Mangels suggested that a reduction might have a less adverse psychological effect than a month ago in view of the fact that there had been some change in conditions. A number of

financial writers, he noted, were analyzing the easing that had taken place through open market operations and were commenting on the possibility of a discount rate reduction. Nevertheless, he would not favor changing the discount rate at this time. There was likely to be some increase in Government spending, along with seasonal pressures, and the System might find itself again having to hold the line. For the same reason, the directive seemed to him to be satisfactory as it stood.

Mr. Deming said there had been no new developments of significance in the Ninth District during the past three weeks. The trend that had been evident for several months continued: modest gains in many measures of activity, appreciably smaller than national gains, and substantial liquidity pressure on the banks. In April, only one major economic indicator--department store sales--showed up better for the District than the nation. In contrast, bank debits were off fractionally from year-ago levels, unemployment was slightly higher than a year earlier, and personal income in Minnesota rose much less than was the case nationally. In agriculture, the season was late but prospects seemed reasonably good. The forecast for winter wheat was quite favorable. Since, in many respects, the lag in the Ninth District reflected the effects of the drought last summer, a good agricultural season, if forthcoming, should change the picture somewhat.

With reference to the discussion of the international and national situation, Mr. Deming said he had no additional comments. As he looked at recent developments, they seemed to support the view that the trend toward

easier money market conditions could be continued without appreciable danger. However, the current uncertainties, in the international picture particularly, argued against any sharp change in policy.

Mr. Deming expressed agreement with the views of Mr. Hayes regarding the discount rate and the directive. He would continue, as Mr. Mangels had suggested, to probe toward easier conditions in the total reserve picture. Like Mr. Irons, he was somewhat confused regarding the development of easier conditions in New York City than elsewhere. He did not see that conditions were appreciably easier in the Ninth District, where the pressure on banks seemed about the same as a month or two months ago. The suggestion that a release of additional vault cash be used as a means of alleviating the situation had some appeal, although he had not thought particularly about this possibility before today's meeting. To summarize his views on the general policy program, he saw no particular danger in probing toward a mildly easier position.

Mr. Allen reported that in recent weeks activity in certain hard goodslines of importance in the Seventh District, including steel, farm machinery, and construction machinery, had been reduced further. The District had been affected more than the nation as a whole by cutbacks in output, as indicated by the fact that in the four weeks ended May 7 new claims for unemployment compensation in the five-State area were 50 per cent above last year, compared with a 25 per cent increase nationally. For the four post-Easter weeks ended May 14, department store sales were

only slightly above last year, both in the country and in the District. For the final two weeks of this period, the District showed declines from last year, possibly accounted for by cold and rainy weather this year and excellent sales last year.

The analyst for the nation's largest retailer of general merchandise found recent trends "confusing," Mr. Allen said. However, this analyst continued to look for a good year-to-year rise and believed that the use of credit by consumers was still moderate in the aggregate and could expand relative to cash sales. Business and financial circles continued to view the future with confidence but without enthusiasm. With few exceptions, capital spending plans were being carried through. The prospect of shrinking profit margins, naturally enough, was cited by some firms as the reason for a high level of capital outlays. Examples were found in petroleum, chemicals, railroads, and food processing. The Purchasing Agents of Chicago continued to report that deliveries of goods were speeding up, and more and more of them found that inventory reduction programs had been completed. That seemed to be the case in steel, as an example. The steel industry nationally was operating at 72 per cent of capacity in mid-May. In Chicago the rate had been a point or two higher than the national rate, and in Detroit operations had been maintained near capacity. Contacts in the industry now estimated that the second quarter rate would average 72 per cent, the third quarter 69 per cent, and the fourth quarter in the 80's.

Auto production continued to increase, Mr. Allen noted, with last week's output estimated at 156,000 as against 146,000 in the prior week.

It appeared that May production might exceed 623,000, and June schedules called for 628,000 assemblies. That meant that despite good sales-- April sales and early May sales were the best since 1955--inventories would continue at a high figure at least through June. On May 10 they were 1,042,000 units, a record high for the industry. Production in the third quarter was scheduled to drop to 1,000,000 cars--450,000 in July, 250,000 in August, and 300,000 in September. The assembly lines would start to go down in July, with most of the down time coming in August. Compact car changes reportedly would be negligible, so on those lines the changeover time would be the shortest on record. And manufacturers would work hard to get out the new models, so September production could run well over the 300,000 projection.

Mr. Allen pointed out that in the past several years the number of passenger cars delivered in the first four months had been just about one-third of the total for the year. In four of the past seven years it had been exactly one-third. If that relationship should prevail in 1960, the number of new car deliveries would be just under 6,300,000. With five or six hundred thousand imports, total deliveries would be at about the 6-3/4 million level that conservative forecasts suggested at the beginning of the year.

With regard to the financial picture in the District, Mr. Allen said that many of the larger banks were in a tight position, at least relatively, the reason being disparity of loan trends. So far this year

the business loans of weekly reporting member banks in Chicago had increased by 7 per cent, in Detroit by 10 per cent, in Indianapolis by 13 per cent, in Des Moines by 15 per cent, and in Milwaukee by 20 per cent. In New York there was a decline of 2.3 per cent. Excluding New York and the five major Seventh District cities he had mentioned, business loans in the rest of the country increased by 3 per cent. Without going into a detailed analysis, the disparity seemed to lie in loans in nonmanufacturing categories, chiefly public utilities, which declined in New York and increased rather generally elsewhere throughout the country.

Mr. Allen said that in view of the conditions in the Seventh District that he had mentioned, he would not favor a change in the discount rate at this time. Mr. Thomas had suggested that the discount rate, at its present level, might be a deterrent to credit extension, but this did not appear to be the case in the Seventh District. For the next three weeks, Mr. Allen suggested continuing to aim at a zero level of net borrowed reserves, although he would not object to $100 million either way. Again having in mind conditions in the Seventh District, he would leave the directive in its present form. In his opinion, the reference in the directive to guarding against excessive credit expansion was appropriate.

Mr. Leedy said that financial and economic indicators in the Tenth District corresponded generally to those elsewhere in the nation, although in some areas the indicators were not quite as favorable as for the country as a whole. This was true, for example, with respect to retail sales, where

the Tenth District was one of those on the minus side this year. There had been a pronounced decline in demand deposits. While unemployment compensation claims were lower than earlier this year, they were still at a higher level than last year.

Mr. Leedy indicated that he continued to be concerned about the money supply and the fact that, notwithstanding the program followed in recent weeks to provide some ease in the reserve position of the banks and in the credit picture, the System was not getting the results that might have been anticipated. The fact that the effects of the breakdown of the Summit Conference could not yet be fully measured must be taken into account. From the analysis presented by Mr. Noyes, there apparently was not much to be feared as far as Governmental expenditures were concerned, but the effects of recent developments on the private sector of the economy were yet to be determined. The performance of the market seemed to him to have been quite reassuring, but whether developments yet to come and further appraisal of what had happened might set off another movement in the direction of inflation remained to be seen.

Mr. Leedy said he would be hesitant to suggest that the System should be moving very much further in the direction of ease or that any immediate step should be taken on the discount rate. Nevertheless, he was concerned about the matters to which Mr. Thomas had referred. The penalty feature of the discount rate and the gyrations in the bill rate indicated to him that the present discount rate level might be operating

to defeat, or at least retard, obtaining the results that had been sought in the program of providing additional reserves. He would favor continuing to make some moderate additions to reserves and, recognizing the difficulties involved in attempting to fix a target in terms of net borrowed reserves, he would leave to the Management of the Account considerable latitude in continuing to conduct operations in accordance with that objective, even if this meant creating some amount of net free reserves. At the same time, he would feel that if, by the time of the June meetings of the directors of the respective Reserve Banks, there had not been any developments, or more evidence than now existed, to indicate that the events of the past week portended something substantial in the way of inflationary bias, consideration might be given to a change in the discount rate.

Mr. Leach reported that Fifth District business activity had expanded moderately in recent weeks, reflecting a pattern of seasonal changes and normal growth. There was virtually no evidence of either speculative expansion or cyclical contraction. District growth was reflected in the good volume and diversity of industrial and commercial building projects planned and in process. Seasonal strength was evident in the District's declining rate of insured unemployment, in the appearance of new activity in textile markets while backlogs were still substantial, and in lumber market improvements. Existing backlogs of furniture manufacturers were estimated to be equal to 3-1/2 weeks' production, which was considered fairly strong. Cigarette manufacturing companies were experiencing good sales and earnings, while bituminous

coal production improved in April and was one per cent above a year ago. On balance, the District farm situation continued to improve, although unseasonably cool weather had made necessary the replanting of considerable cotton acreage.

At Fifth District banks, Mr. Leach said, loans continued to rise more than seasonally. During the past three weeks, they had increased by a larger percentage than during any corresponding period since 1955. The discount window continued active and banks had been net purchasers of Federal funds.

With respect to open market operations, Mr. Leach said he would continue to maintain the present posture and not lean in either direction. Any further easing might invite trouble, and maintenance of the status quo should provide such reserves as were needed to support economic growth. He would expect net borrowed reserves to be around zero. Developments in the past three weeks had not caused him to change his opinion as to the discount rate; he would prefer to stand pat for the time being. As he had said before, he felt that the expression "while guarding against excessive credit expansion" had been inappropriate for several weeks and that it should be omitted from the directive. Nothing in today's economic report made him fearful of inflation in the immediate future.

Mr. Mills said the facts that the level of outstanding Federal Reserve credit was no higher than a year ago, the level of required reserves was lower, and the velocity of the turnover of money was maintained at a

high rate convinced him that the money supply continued to be under heavy pressure and accounted for the fact that the money supply remained at a figure below a year ago. In the light of those facts, it seemed to him that the Federal Reserve System was called upon to provide additional reserves through some vehicle that would help to sustain the increase in gross national product and the higher level of personal income, to the end that, it would be hoped, the expansion in economic activity being looked for in some areas would be achieved. Listening to the discussion around the table, he was impressed that there were so many who seemed to feel that the System was groping in the dark for an understanding of the financial situation, and particularly the factors that affect the commercial banking system in the utilization of the reserves supplied to it. To add his speculation as to the reasons for the perplexity, he thought it not improbable that in hindsight attention would be focused on the attitude of the commercial banks, as a reflection of their investment and lending positions. Mr. Thomas had developed the imponderables relative to the Federal funds situation and, more importantly, an area that deserved much greater investigation and analysis, namely, the volume of bank borrowing that originates outside of the Federal Reserve Banks and the Federal funds market. It was his impression that the volume of such borrowing was tending to increase, that it had moved fast into the reserve city banking picture, and that it was now moving rather rapidly into the country bank sector, particularly in the case of country banks that found themselves

handicapped in meeting the loan demands of their communities in the face of a leveling-off or loss of deposits and were turning as a consequence to borrowing from their correspondent banks, since Regulation A properly does not encourage more than temporary borrowing from the Federal Reserve Banks. It was his impression that there was a backing up of general borrowing demands from the country banks to the reserve city banks, thus exerting a depressive influence on their credit activities. If the System should see fit--and he believed it would be advisable--to supply additional reserves and bring negative free reserves down to the zero level, or perhaps to bring about some free reserves, he considered it doubtful that the effect of those reserves, as they reached the commercial banking system, would be other than beneficial, for he felt that the commercial banking system required some leeway in order to meet a reasonable loan demand that was reaching the banks. As that loan demand was pressing against their loan-to-deposit ratios, the banks were not encouraged to expand credit aggressively. In consequence, if reserves were more freely available, one might reasonably expect some increase in loans, and beyond that an expansion of holdings by banks of short-term Government securities. This in turn would afford the banks a certain psychological easiness in their attitudes and give them less discomfort about their high loan-to-deposit ratios. Parallel to a development of that sort--and the symptoms might already be appearing at the New York City banks--he thought it likely that the commercial banks would act to put their houses in order and reduce their outstanding credit commitments, while at the same time meeting

the necessitous demands for credit that were properly brought before them. In other words, such a dovetailing of influences--a reduction of commitments and a reduction of loans in some areas while, on the other hand, the banks justifiably and properly serviced credit demands that commercial banks have an obligation to meet--might bring about a proper increase in the level of commercial bank loans while at the same time the banks were curtailing their credits in other areas. Thus, there was not likely to be the kind of credit expansion that would arouse concern from the standpoint of inflationary influences. In short, he saw little need to be concerned that an increased supply of reserves would spark any expansion of bank credit that would be other than helpful to the economy at the present time.

Mr. Mills noted that in countries abroad, particularly the United Kingdom and to a somewhat lesser extent, perhaps, Germany, the Low Countries, and Japan, the forces of business expansion appeared to be approaching a point that was requiring more aggressive attention from the monetary authorities. It seemed to him that at some point not too far in the future the effects of those restrictive policies would be reflected in United States exports and that the volume of exports might fall to a degree. If and when that came about, it would be a matter of serious concern in the United States, because along with that development there were reasonable possibilities that the lack of aggressive expansion of domestic economic activity would be followed by a substantial contraction of imports. Accordingly, he suggested that it might be advisable if the economic staff would develop some projections

that might reveal the extent to which a contraction of imports could proceed without producing a reversal in the dollar and gold positions of friendly neighbors and compelling a flow of gold to this country that might be embarrassing to them. In view of the substantial time lag from the date of origination of export and import transactions to their reflection in balance-of-payment statistics, he also suggested that it would be desirable to obtain some sense of what was going on in both domestic and foreign business communities as to forward commitments that in due course would affect the international balance of payments.

Mr. Mills said he would not be inclined to favor a reduction of the discount rate until about the time of the next Committee meeting, at least. If, by that time, additional reserves were supplied in reasonable quantity, the System might be in a better position to assess the impact of those reserves on the financial markets. He would not change the directive at this time.

Mr. Robertson said that in view of the international situation and in the absence of any strong trends domestically, either up or down, he would agree with those who had spoken in favor of maintaining present policy for the time being, neither easing nor tightening. It was a position that he would consider quite neutral. He was grateful to Messrs. Thomas and Irons for the suggestions they had made with regard to the discount rate and vault cash. He had the feeling that by the time of the next Committee meeting consideration perhaps should be given to a change in the discount rate,

depending entirely on what happened in the interim. He also felt that there should be exploration of the proposal of Mr. Irons with respect to supplying reserves through instruments of policy other than open market operations in a way that would scatter them throughout the country.

Mr. Shepardson expressed the view that the economy, in general, seemed to be moving along in satisfactory fashion. Thus far, there had been no evidence of undue disturbance because of recent international developments, although some uncertainty was bound to exist. At the time of the May 3 meeting, Mr. Shepardson recalled, he had the feeling that by this time serious consideration should be given to a change in the discount rate. Because of the current uncertainty, however, he was not sure. He still thought there would be some advantage in a change in the rate, but in view of the present situation it might be appropriate to defer consideration of a change for some little period. He felt that the discount rate, at its present level, was having an effect on the distribution of funds, as Mr. Thomas had pointed out, and the lack of growth in the money supply continued to give him some concern. If no change was to be made in the discount rate, he believed that it would be desirable to continue to supply reserves through open market operations, looking toward a zero level of net borrowed reserves, plus or minus. This would mean reaching somewhat further in the direction of supplying reserves than contemplated by the consensus, as he recalled it, at the May 3 meeting.

Mr. Shepardson commented that, like Mr. Leach, he had felt at the past two meetings that it might be well to change the directive to eliminate the portion of clause (b) having to do with guarding against excessive credit expansion. He still thought such a change would be appropriate, with perhaps a substitution of language along the lines suggested by Mr. Johns at the May 3 meeting.

Mr. King noted that those who had spoken today apparently were in general accord. His own thoughts, he said, were in line with those expressed by the group as a whole. In terms of net borrowed reserves, he felt that the Committee should aim at zero and try to work in that general area.

Three weeks ago, Mr. King recalled, he had said that he would be inclined to approve a change in the discount rate if a majority of the Reserve Banks wanted to move on the rate. At present, he was inclined to feel that it would be better to defer such action for some time, at least, and reconsider the matter in the light of circumstances as they might develop a few days in the future. Like Mr. Irons, he believed that the effects of open market operations had not reached out very far from the New York City banks. In his opinion, therefore, the suggestion of Mr. Irons in regard to a further release of vault cash was worth exploring.

In further comments, Mr. King repeated that as of today he would leave the discount rate alone. He felt that the System would have been in

a better position to have moved on the rate three weeks ago. At present, he thought the System would be well advised to sit tight on the rate and to continue easing the reserve position of the banking system through open market operations. As he had indicated, he would try to reach a zero level of net borrowed reserves. He would favor deleting from clause (b) of the directive the phrase having to do with guarding against excessive credit expansion.

Mr. Fulton said that in the Fourth District there were a few favorable developments, including a high level of new auto sales, an increase in the output of coal, and a higher volume of construction than last year, with the increase largely in the industrial field. Unemployment had declined, but not as much as seasonally, and some pockets of substantial unemployment remained. The situation with respect to heavy industries might be characterized as one of "deteriorating stagnation." Nationally, the rate of steel production for this week was projected at about 67 per cent of capacity; in the District the projections ranged from 41 per cent in Youngstown to 76 per cent in Cleveland, where the rate was admittedly high and was expected to go lower. At present, expectations were that during the holiday week of July 4 the rate of steel production might go as low as 50 per cent nationally. New orders were deteriorating rapidly and were coming in at a rate of only about 50 per cent of capacity. Steel men claimed that the inventory liquidation among their customers was the most rapid in their experience. They did not know when the situation would level off, although it was felt that the

automobile industry might begin to order in the latter part of July. In the case of some steel customers, it was indicated that the use of computers was enabling them to control inventories more precisely than in the past. Thus, they would tend to keep inventories at a minimum, expecting that the mills would be able to deliver promptly whatever was required. In the next ten days, several thousand workers at one mill were scheduled to be laid off because of a declining order book.

Mr. Fulton commented that an unfavorable inventory situation prevailed among the auto parts manufacturers, who had scheduled their operations in line with the substantially higher rate of output anticipated by the auto companies earlier in the year. Now that the auto companies were dealing on a 20-day inventory basis instead of a 45-day basis, these parts were being carried by the manufacturers and their operations were quite low. Appliances were overstocked, and machine tools and heavy machines were not moving well. The orders that had been anticipated incident to plant and equipment expenditures had not appeared; there were, reportedly, lots of plans, but there were few firm orders.

All in all, Mr. Fulton said, the picture in the Fourth District was not bright for the next couple of months, at least.

Mr. Fulton expressed the view that more reserves were needed, that the supply had been starved to a considerable degree, and that the aim should be a situation from zero up to $100 million of free reserves. He did not feel that net borrowed reserves were appropriate at this time. The country (agricultural) banks particularly were in a tight situation, and there was a good

demand for loans. If the loan demand was not satisfied to a degree, a psychology might develop that could be cumulative in its effect; and if such a psychology developed, it might be difficult to reestablish loan demand once it had stopped.

Mr. Fulton agreed with Mr. Irons that the distribution of reserves was not good and that an adjustment of reserve requirements by way of permitting additional vault cash to be counted as required reserves might be a highly appropriate means of achieving a better distribution. It appeared to him from the projections that substantial quantities of reserves would be needed in the near future, and it might be appropriate to provide them in this way.

Mr. Fulton pointed out that borrowings of member banks from the Reserve Banks had been at a rate around $500 million for some time, and he noted that the banks probably would want to get out of debt to the Federal Reserve rather than employ their funds for lending purposes when additional reserves became available. The present degree of restraint seemed to him a little too strong in the light of what he viewed as a deterioration in the psychology of business. For reasons already stated by others, he would not change the discount rate at this time. However, he felt that it would be appropriate to change the directive by deleting the portion of clause (b) that referred to guarding against excessive credit expansion.

Mr. Bopp said that conditions in the Third District were not as good as nationally, and the national movement had been described as sideways. Turning to the discount rate, he reported that the directors of the Philadelphia Bank, at their meeting on May 5, felt unanimously that the discount rate should be reduced. They went along unanimously with continuing the present rate only as an expression of confidence in management, perhaps, and because the Treasury was in the market at about that time. At the meeting last Thursday the directors again voted unanimously to continue the existing discount rate, but only because of the international situation, which still required interpretation and might have led to a revival of inflationary pressures. The directors felt unanimously that in the economy as a whole there were very few bottlenecks. Looking at plant capacity, employment levels, industrial production, and prospects for the immediate future, they concluded that there was adequate capacity to permit a significant increase in output without the danger of strong inflationary pressures developing. On the basis of this appraisal of the domestic economy, they felt that a discount rate reduction would be appropriate.

Mr. Bopp said that he agreed with the directors. Although he appreciated the possible results of recent international developments, it appeared as though the country had taken those developments pretty much in stride. If a reduction were made now in the discount rate and inflationary pressures should revive, the System could always move in the

other direction. A reduction would indicate that the System was flexible and did not always tend to lean in the direction of tightness.

After indicating that he had been impressed by the analysis presented by Mr. Thomas concerning the sources of funds, Mr. Bopp outlined the general picture that he would like to see develop. This embraced a position of free reserves, the Federal funds rate periodically, at least, below the discount rate, and member bank borrowings less than $500 million. He would recommend reducing the discount rate one-half point, and he would delete the portion of clause (b) of the directive which referred to guarding against excessive credit expansion.

Mr. Patterson reported that Sixth District indicators showed signs of some improvement in business activity although there were many mixed movements. Nonfarm employment was up in April and department store sales doubled the rate of increase for the nation as a whole. While construction employment was down in March, the fact that awards increased in January and February pointed to possible improvement in construction employment. The late cold spell resulted in estimated damage to the cotton crop of $4 to $6 million, but the farm production outlook was still relatively good. Farm wages were higher than last spring, although rates were still 9 per cent below farm wages elsewhere in the nation. Farm marketings were being maintained at a higher level in the District than nationally.

Turning to District banking developments, Mr. Patterson said that lending rose in April and then declined slightly early in May.

Deposits rose modestly in April. Borrowings of member banks in relationship to the System total were still high.

Mr. Patterson said that few complaints had been heard from commercial bankers with regard to monetary policy. However, many bankers had expressed the view that the legislation passed by Congress last year to permit the carrying of vault cash as part of required reserves was intended to produce some benefit to the banks and that they had gotten little from the present allowances.

Mr. Johns said he continued to hold the views that he had expressed at the May 3 meeting. He thought it highly desirable for such additions to be made to the supply of reserves as would in time, it might be hoped, be reflected in an increase in the money supply. In this connection, he wished to make the point, as he had done repeatedly on previous occasions, that in his view the use of net borrowed reserves as a proximate objective of monetary policy might lead to results that were not wanted and not intended. This he felt it had done in recent months, for the reason, primarily, that a net borrowed reserve target leaves out of account the question of what the banks do with the reserves that are available. The evidence seemed quite clear, as Mr. Thomas had pointed out, that when the reserves are used to reduce indebtedness to the Federal Reserve Banks, the System does not obtain the result in total reserves or the money supply for which it is aiming.

Mr. Johns said that in recent days banks in the Eighth District had decreased somewhat their use of the discount facility, measured both

in terms of number of banks borrowing and in dollar amount. However, he felt it would be quite erroneous to construe this as evidence that the banks felt easier or were in fact in an easier position. The disposition of Government securities continued, but there was also another factor involved. Some of these banks had been rather steady customers at the discount windows of the Reserve Bank. In some cases, there had been tactful discussion with those banks of their situation and plans for the future; in other cases, the banks well knew the time was approaching when they might expect similar approaches from officers of the Reserve Bank. This was particularly true in Memphis, where the cotton financing banks continued to be under pressure but had gotten out of debt to the Reserve Bank. Mr. Johns added that he wished to underline what Mr. Thomas had said about the indebtedness of banks to other banks and to nonbank lenders. This had been observed for quite a time.

In the circumstances, Mr. Johns said, he would like to see instructions issued to the Desk that would bring about an increase in the total supply of reserves, in the hope that sooner or later this would result in increases in the money supply. He again wished to caution that if the Committee adhered too closely to a net borrowed reserve target this objective might be defeated.

Three weeks ago, Mr. Johns recalled, he had expressed the view, for reasons to which Mr. Thomas referred today, that the discount rate ought to be reduced, and he had suggested a reduction of one-half point as soon as

possible. This was not intended, however, to be taken as meaning that a reduction should necessarily be made right at that time. At the meeting of the directors of the St. Louis Bank a few days later, he did not recommend a reduction, for he had in mind the traditional policy of even keel during a period of Treasury financing. Similarly, when he said today that the discount rate was in need of downward adjustment, he was quite aware of the fact that there had been a radical change in the international situation. Therefore, although with some regret, he would be quite prepared to accept a further deferment of action on the discount rate rather than to take such action too hastily without full realization of the impact of the international situation. For his own part, he was inclined to think that the impact on the economy would not be too great and that before long the System might see its way clear to make the downward adjustment of the discount rate that he thought was needed.

Mr. Johns said that he would still like to see the directive changed in the manner he had suggested three weeks ago, so as to remove what he considered undue and inappropriate emphasis at this time on guarding against excessive expansion of credit.

Mr. Balderston said the rolling prosperity that he thought descriptive of the economy three weeks ago seemed to be continuing to roll, and on a high plateau. However, he did not see ground ahead that was higher than the plateau on which the economy had been travelling. Steel production was down, rental vacancies were up, and unemployment rates were unsatisfactorily high

in relation to the current phase of the business cycle. Consequently, believing as he did that the System should take action earlier rather than later, even though it might not want to make overt moves, he would favor a change in the directive. It seemed to him three weeks ago that monetary policy had changed, and that it was being changed even more at that time. Accordingly, he felt that it would be appropriate to make one of two changes: either to eliminate from clause (b) of the directive the phrase "while guarding against excessive credit expansion" or to substitute some modification of clause (b) along the lines suggested by Mr. Johns at the May 3 meeting. He was inclined to favor the latter alternative and therefore would like to suggest an amendment of clause (b) so as to provide for operations with a view "to fostering sustainable growth in economic activity and employment while increasing moderately the total reserves of member banks."

With regard to the target for open market operations, Mr. Balderston said he would consider a target of free reserves of at least $100 million appropriate. He was deeply concerned that the efforts the Committee had been making to increase the money supply had thus far proved ineffective. His conclusion was that the loaned-up condition of the banks and the expectation of heavy loan demands upon them during the fall had created a psychology among bankers that tended to make the current level of reserves operate in a different fashion than had been the case some years ago when the ratio of loans to deposits was lower. In short, he was not sure that

a zero level of net borrowed reserves would increase the money supply promptly, and he felt that the System must seek some results promptly. He would, therefore, like to see free reserves at once, and in the amount of at least $100 million. He was rather impressed with the suggestion of Mr. Irons that another move might be made to increase the portion of vault cash countable as required reserves. He was not certain whether that should be done during the next month or until the System found it appropriate to change the discount rate. Nevertheless, he thought the idea was well worth studying.

Chairman Martin said it seemed to him that the only added starter at this time, as compared with the May 3 meeting, was the international situation. It was too early to attempt to evaluate with any degree of certainty the effects of the breakdown of the Summit Conference. However, it was his feeling that the evolution of Federal Reserve policy was quite clear; it had been moving in a clear direction. If he understood correctly, nobody today had indicated a desire to tighten, and the question, therefore, was how to increase the money supply, and when, under present conditions.

The Chairman said he did not think there was evidence of any strong upward pressure on prices at the moment. He thought the Committee could find some satisfaction in the way it had been increasing reserves in the market, but there was reason for concern about the lack of response of the money supply. In his opinion, this could not be corrected overnight, but it was necessary to face up to some fundamentals. The most significant

unexplained item in the first half of the year, to date, had been the decline in interest rates, that is, the way it came about. There had as yet been no satisfactory explanation of that development, but it convinced him that something had been going on in the economy. While he did not want to sound too bearish, his choice of one word to describe the present situation would be "saturation." As he saw it, the economy was in a period of temporary saturation, of which the automobile market was an indication. Despite good sales of cars, some unemployment might be seen in that and other areas before long, because for the time being the market was saturated. A new demand must be developed for some products.

In certain respects, Chairman Martin said, he thought the System must reorient its thinking. The situation with respect to the balance of payments disturbed him. He was not optimistic about the longer-run aspects of the balance of payments, and he was not completely convinced that one could totally ignore world money markets. To pursue any policy such as in 1957 and 1958 would be disastrous. There could not be moves of that sort, where the only significant development in the economy was a decline in interest rates. Looking back at the recession of 1957 and 1958, that was about all that occurred. Instead, there must be adjustments in prices in some areas, although admittedly this would be painful. As he had mentioned before, the profit margin was becoming more of a problem.

Chairman Martin recalled that he had been firm at the May 3 meeting in saying that he thought it would be a mistake to adjust the discount rate.

Basically, he believed that the international situation was a disturbing element to business planning, and not the reverse. If a firm were considering plant and equipment expenditures, and the development of markets, the management would not be thinking primarily of inflationary consequences at this particular juncture. Instead, the thinking would be likely to center on the prospect of an extension and intensification of the cold war, with no prospect of a break in the situation for some time. In these circumstances, such a firm might well be inclined to be more cautious and less likely to spend. This, Chairman Martin added, was a tentative judgment, and the matter could be argued on both sides of the fence. He was merely throwing this out as his own tentative thinking.

After referring to the gyrations of the bill rate, the Chairman said that the situation seemed to call for some adjustment of the discount rate. It would be preferable to have another ten days, or possibly two weeks, to digest the international news before taking overt action. However, net borrowed reserves were already down to around the zero level. In fact, free reserves were indicated, on average, for the current statement week. If it was the intention of the Committee to supply additional reserves--and the sentiment around the table today so indicated--this would put more pressure on the discount rate as time passed. While he did not know at what point the supplying of additional reserves would take hold, the market process was perfectly clear. It was only a matter of time before it would become necessary to face up to that.

In his opinion, Chairman Martin said, the System should continue to feel its way; the odds were all with the System. He found himself influenced by the sentiment around the table in favor of moving, slowly and cautiously, in the direction of supplying additional reserves. At some point the money supply would begin to take hold, and then the System could consider what ought to be done.

In further comments, the Chairman alluded to the difficult problems confronting the System in the psychological area. There had recently been speculation, he noted, regarding a reduction of margin requirements. He did not know what the manifestations of that would be, but there would be a difficult problem of explanation. In either a further release of vault cash, a possibility to which he had been attracted for some time, or a direct cut in reserve requirements, there would be a difficult problem of explanation because the broad problem was not generally understood. A lot of people who favored an easy money policy some time ago were now for a tight money policy because of the problem of the balance of payments. In his opinion, they were grossly exaggerating the impact, but without doubt there were cross currents and swings.

Chairman Martin repeated that he felt the System had been moving in the right direction. It would be helpful to have a better chance to digest what was coming out of the breakdown of the Summit Conference and the effects on the domestic economy. At the same time, the summer doldrums were now rather close at hand. In his view, the Committee would be justified

on that basis alone in moving in the direction of supplying additional reserves.

Chairman Martin then said that if open market operations were going to move into the direction indicated by the consensus it would seem to him to make good sense to change the policy directive. Mr. Balderston had made a suggestion, as had several others. He (Chairman Martin) had before him a suggestion of Mr. Thomas, which was that clause (b) be amended to provide for operations with a view "to fostering sustainable growth in economic activity and employment by providing reserves needed for moderate credit expansion." This, he noted, would be a simple, straightforward statement; it would not state how much would be done or in any way say that the Committee would necessarily do anything or change anything.

The Chairman then called for discussion and, in the light of a comment by Mr. Shepardson, the suggestion was made that the word "bank" be inserted just prior to the words "credit expansion."

Mr. Robertson noted that an alternative would be to strike the language of the existing clause (b) after the word "employment" so that the clause would read "to fostering sustainable growth in economic activity and employment."

Mr. Shepardson then moved that clause (b) be amended to read "to fostering sustainable growth in economic activity and employment by providing reserves needed for moderate bank credit expansion", and this motion was seconded.

Mr. Hayes noted that Committee policy had been changing only gradually and said it would be his preference that the directive also change gradually. The thing that some members of the Committee had been wanting to get rid of was the portion of clause (b) relating to guarding against excessive credit expansion. He wondered whether the proposed change might not represent too much of a jump at one meeting, and whether the Committee should not remain on more neutral ground for a while.

Mr. Johns asked what a more liberal supplying of reserves was intended for, if not to provide reserves needed for moderate bank credit expansion, and Mr. Irons stated that his objection to the shorter form of clause (b) mentioned by Mr. Robertson would be on the ground that the language was so broad it could almost never be changed.

Chairman Martin suggested that each of these statements should be looked at in the context of what the Committee had been doing in the past several weeks, following which Mr. Hayes said he had been concerned for a long time about the fact that clause (b) typically contained long-run goals as well as more immediate objectives. He suggested that appropriate members of the Committee's staff might be asked to work on a method of separating the two parts of clause (b); that is, the more permanent part and the temporary objective.

Chairman Martin replied that this would represent a somewhat longer-range project. He felt that the Secretary of the Committee could well be asked to work on improving the form of the directive; that is, the way in

which the directive is cast. However, for the immediate purpose of the meeting today, the question was one of deciding whether clause (b) of the existing directive should be changed in the manner that had been suggested. The Chairman then read again the proposed change in clause (b) that had been moved and seconded.

Turning to the level of reserves, Chairman Martin said it seemed clearly to be the consensus that the Committee should not tighten and that it should continue in the direction of a modest increase in the supply of reserves.

In this connection, Mr. Shepardson clarified that his thought had been to provide an increase in the supply of reserves. In making his earlier statement, he had had in mind that the target at the May 3 meeting was in terms of a range from $100 million of net borrowed reserves down to zero. If it would make his position clearer, he definitely contemplated some further increase in the supply of reserves.

Mr. Allen said that, as he understood it, the consensus at the May 3 meeting was in terms of trending toward zero, and Chairman Martin said the suggestion today would be to carry that a little further.

Chairman Martin then referred back to the change in the directive that had been moved and seconded, and inquired whether anyone wished to record a negative vote. There being no such indication, he stated that the directive would be approved in such form. He also stated that the consensus would be to trend slightly further in the direction of providing reserves.

Mr. Balderston inquired whether the consensus would be interpreted by the Desk as meaning net free reserves rather than net borrowed reserves, and Mr. Rouse said he thought this was understood.

Accordingly, 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 by providing reserves needed for moderate bank 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.

With further reference to the discount rate, Mr. Shepardson said he hoped that as the situation clarified, particularly the international situation, and unless there was an unfavorable turn of events, consideration might be given to a change in the rate before the next Committee meeting.

Mr. Hayes noted that the discount rate was not within the scope of the consensus reached at Open Market Committee meetings, and Chairman Martin agreed that the role of the Committee was purely advisory, with neither the Board nor the Presidents being committed.

Mr. Hayes then said he thought it proper to emphasize that a large majority of those who commented today had indicated that they would not favor moving on the discount rate now. Also, he wished to point out that advance refunding by the Treasury of the 2-1/2 per cent bonds of 1961 might be in the wind. As of now, there was a question whether this might be done before the next Committee meeting. He also mentioned again, as a factor to be considered, that the System should have in mind the position of friendly foreign countries; he felt that this factor deserved some weight.

Chairman Martin said that without question this factor was involved. He added, however, that the System could not let the problems of foreign countries compound its own problems, and Mr. Hayes said that he granted the point.

Chairman Martin repeated that he thought the role of the Federal Open Market Committee in relation to the discount rate was clearly understood. Discussion within the Committee does not bind any President or any member of the Board of Governors.

The Chairman went on to say that this was an evolving situation, and that the System must tackle it as it moved along. That was the framework

in which it was necessary to work at the present time. It might be that a week from today nobody would want to do anything on the discount rate but that in two weeks, for example, the situation might be different. He went on to say that the more time the System could have to digest developments the better it would be, and that the System would not want to jump prematurely. The more time it could get and the more orderly a manner in which it could take things, the better off it would be. On the other hand, things cannot always be ordered in a way that one would like to see them. The System cannot set dates and be bound by them.

Mr. Bopp commented that at a number of Reserve Banks it is the practice of the Board of Directors to meet only once a month. This presented a technical problem of a complicating nature.

Mr. Hayes said he had always considered it desirable that timing of discount rate actions be coordinated, and that it had been his feeling that a consensus on the rate at the Federal Open Market Committee meetings had been helpful in achieving this coordination. The general feeling today appeared to be that a change in the rate would not be a good idea.

Chairman Martin said that the view of Mr. Hayes was well expressed. As he had indicated previously, however, discussion of the discount rate at Open Market Committee meetings could not be binding upon anyone.

Mr. Balderston expressed agreement with Mr. Hayes that time might help to clarify the situation internationally in this particular field. However, as far as Treasury operations were concerned, he noted that a

reduction of the discount rate was a different thing from an increase. In the fall of 1957 the Treasury postponed a financing operation temporarily, if he remembered correctly, because the Federal Reserve System was prepared to decrease the discount rate, but there was only a short interval between the two actions. Had the System been moving in the opposite direction, it would have been an entirely different matter.

Mr. Bopp pointed out there are relatively short, and few, intervals when the System is free to move on the discount rate. If the Treasury should take up these intervals by advance refunding or similar operations, the opportunities for discount rate action would become very limited.

Mr. Robertson commented that if there was to be a move on the discount rate, that move should be made not after advance refunding took place but before such time, and Messrs. Balderston and Bopp expressed agreement.

Chairman Martin suggested that the attitude of the System be one of flexible, watchful waiting. In a further comment, he issued a word of caution that all those present be most careful in their conversations after they left the room today.

Chairman Martin then referred to a memorandum from Mr. Rouse dated May 20, 1960, which transmitted a memorandum of the same date from Mr. Larkin, Assistant Vice President of the Federal Reserve Bank of New York, summarizing operations under the authorization given by the Open Market Committee at its meeting on April 12, 1960, and renewed at the meeting

on May 3, 1960, to acquire up to $150 million of one-year Treasury bills maturing July 15, 1960, either by outright purchase or by swapping other Treasury bills. Mr. Larkin's memorandum indicated that a total of $91.5 million of the bills maturing July 15, 1960, had been acquired under this authorization, so that total holdings of such bills, including holdings of $13.4 million acquired by outright purchase prior to April 12, 1960, amounted to $104.9 million.

Mr. Rouse commented that if the Treasury was successful in developing a better cash position so that it could cut down by $500 million when it came to the rollover, the present holdings of the bills due July 15, 1960, would probably be sufficient. On the other hand the situation was not clear. Therefore, he would suggest that the outstanding authorization for acquisition of the July 15 bills be renewed. Under it, he noted, there was still leeway to acquire up to $58.5 million of such bills.

Chairman Martin inquired whether anyone had heard of repercussions in the market because of the transactions in the one-year bills, and no comments were heard. Mr. Rouse said it was in a way rather strange that there seemed to have been no market comment, because the swap transactions that had been undertaken could clearly be identified in some cases as swaps.

Mr. Thomas noted that the outstanding Committee authorization was limited to acquisition of July bills, to which Chairman Martin added that the Desk was limited to the July bills as far as the acquisition of one-year bills by swap transactions was concerned. Mr. Rouse agreed, stating that,

as far as outright purchases were concerned, it was his understanding that the Account had authority to acquire other issues of the one-year bills, and no disagreement with this comment was heard.

Mr. Hayes said he supposed that at some time the Committee would wish to consider authorizing acquisition of the one-year bills of October 17, 1960, on a basis similar to the authorization relating to the July 15 bills. However, he thought there was no hurry to consider that matter.

Mr. Rouse expressed the view that the operation in the July 15 bills should first be completed so that the Open Market Committee might make an appraisal as to whether it wanted to authorize further operations in one-year bills along the lines of the current authorization.

> Thereupon, it was agreed to renew until the next meeting of the Open Market Committee the authorization given on April 12, 1960, and renewed on May 3, 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. Mr. Robertson dissented from this action to the extent that it involved acquisition of the one-year bills by swap transactions, as opposed to outright purchases.

It was agreed that the next meeting of the Federal Open Market Committee would be held on Tuesday, June 14, 1960, and that the succeeding meeting would be held on Tuesday, July 5, 1960.

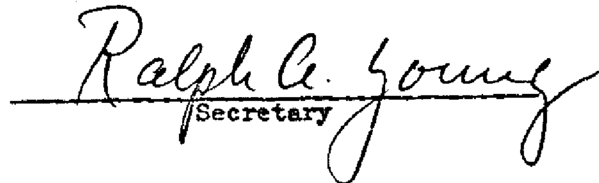
Chairman Martin noted receipt of a letter from Mr. Hayes which suggested that he might want to call to the attention of the members of the Committee and the Presidents not currently serving thereon that the

New York Bank would welcome visits to the Desk. The Chairman said he would like to support this invitation to learn firsthand what was going on at the Desk whenever visits could be worked out.

Mr. Hayes said his thinking was in terms of rather extensive visits, perhaps in the order of a week, during which members of the Committee could sink their teeth into the operations of the Desk and see what was actually going on there.

Chairman Martin noted that three Reserve Bank Presidents (Messrs. Hayes, Allen, and Mangels) had been called to testify before the Subcommittee of the House Banking and Currency Committee that was to hold hearings in connection with H.R. 8516, which would provide for the retirement of Federal Reserve Bank stock.

The meeting then adjourned.




Secretary