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, January 10, 1961, at 10:00 a.m.

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

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

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

Mr. Young, Secretary
Mr. Sherman, Assistant Secretary
Mr. Kenyon, Assistant Secretary
Mr. Hexter, Assistant General Counsel
Mr. Thomas, Economist
Messrs. Brandt, Eastburn, Marget, Noyes, 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. Knipe, Consultant to the Chairman, Board of Governors
Mr. Yager, Economist, Division of Research and Statistics

Mr. Wayne, First Vice President, Federal Reserve Bank of Richmond
Mr. Hickman, Senior Vice President, Federal Reserve Bank of Cleveland

Messrs. Ellis, Baughman, Jones, Parsons, Coldwell, and Einzig, Vice Presidents of the Federal Reserve Banks of Boston, Chicago, St. Louis, Minneapolis, Dallas, and San Francisco, respectively
Mr. Garvy, Adviser, Federal Reserve Bank of New York
Mr. Stone, Manager, Securities Department, Federal Reserve Bank of New York

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

Under date of December 16, 1960, there had been sent to each member and alternate member of the Federal Open Market Committee, and to each President not currently a member of the Committee, a copy of the report of audit of the System Open Market Account made by the Division of Examinations of the Board of Governors as at the close of business October 21, 1960. The report, which has been placed in the Committee's files, was submitted to the Secretary of the Committee under date of November 30, 1960, in accordance with the action of the Federal Open Market Committee at its meeting on June 21, 1939, as reaffirmed most recently at the meeting on March 1, 1960.

Chairman Martin inquired whether any of the members of the Committee wished to comment on the report, and there was no indication to such effect.

Accordingly, the audit report was noted and accepted without objection.

Before this meeting there had been distributed to the members of the Committee a report of open market operations covering the period

December 13, 1960, through January 4, 1961, and a supplementary report covering the period January 5 through January 9, 1961. Copies of both reports have been placed in the files of the Committee.

In supplementation of the written reports, Mr. Rouse commented as follows:

> The past four weeks have witnessed pervasive ease in the money market. At the same time, short-term interest rates have not been unduly depressed. The rate on three-month Treasury bills, for example, moved no lower than 2.16 per cent during the period despite the fact that open market operations provided a large volume of reserves toward the close of the year. With short-term rates remaining relatively stable, there does not seem to have been any strengthened incentive to transfer short-term funds to other markets. The spread between the British bill rate and the Treasury bill rate here on a covered basis has fluctuated from slightly below 1 per cent to a high of around 1.20 per cent in favor of British bills. We cannot measure accurately the actual shift of short-term money in response to interest rate differentials, but we have the impression that relatively little has taken place recently. The sizable foreign purchases of gold in the past two or three weeks point up the fact that this problem is still very much with us. These recent purchases, it appears, represent in good part a conversion of existing assets rather than an accumulation of new assets.
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> The year-end pressures that normally make it difficult to keep the money market easy over the approach to the year end have been mostly absent. Federal funds have traded well below the discount rate through most of the period and bill rates have fluctuated within a narrow range. While foreign accounts and some corporations have liquidated bills, these sales seem to have been about offset by demand from banks and other corporations. We see some evidence that banks are putting their ample surplus reserves to work in Government securities to a greater extent, and in some cases are undertaking a modest amount of maturity extension. However, the attitude of investors in fixed income securities generally is clearly one of caution.
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> Funds were injected through open market operations mainly by way of repurchase agreements, mostly at 2-3/4 per

cent in order to compete with other sources of funds and to encourage the dealers to leave the contracts on the books. Through this measure it has been possible to avoid outright market purchases of Treasury bills even though the contracts have not remained on the books as long as we would have liked. We did, however, purchase some Treasury bills from foreign accounts. Earlier in the period reserves were absorbed through sales not only of bills but also of short-term securities other than bills. Most of these sales were made to the International Monetary Fund, which was investing the proceeds of its recent sale of gold to the Treasury.

Prices in the Government securities market moved generally upward over most of the period, but underwent sizable declines in the past few days. These declines reflect renewed doubts as to the duration of the business recession and more active discussion of the gold outflow as a symptom of our unfavorable balance of payments--developments which have occurred against the background of the heavy positions accumulated by dealers. Total dealer positions reached a peak of $3.8 billion, an all-time high. These positions, which were largely in short-term issues, include securities held under long-term repurchase agreements. Although dealer holdings have subsequently been reduced, they are still at a level that could be troublesome in the event of some unforeseen development, such as a marked worsening in the international situation.

The Treasury is again facing new financing operations, first in the roll over of the January 15 bills through an auction tomorrow, which we expect will be routine. The next operation will be the refunding of the February 15 maturities, which presents some problems, such as whether to refund through a cash offering or through the normal exchange technique, and also whether to attempt a further extension of maturity at this time. The problem of maturity is a difficult one, since there are already outstanding about $11 billion of securities maturing in February 1962. These decisions, of course, will be made by the incoming Treasury team, but with the advice and counsel of the outgoing team to the extent that it is wanted.

As I have noted in previous reports to the Committee, the market for bankers' acceptances continues to grow. Both in October and November the total of acceptances outstanding surpassed the previous high established some thirty years ago, and there is some likelihood that the December figures, when they become available, will show further growth. Toward this past year end the dealers in acceptances were called upon to absorb larger amounts of these obligations than ever before.

> But in the easy money market conditions prevailing they have been able to handle this large volume of acceptances without strain and to market them in orderly fashion to a wider assortment of domestic buyers than at any time in the past.

Mr. Erickson referred to the very large holdings of Government securities by dealers and asked how those holdings would be handled if the demand anticipated by the dealers did not materialize and the System was not in a position to put reserves in the market.

Mr. Rouse replied that the major problem, in view of the shortness of the maturities held, was the availability of credit to enable the dealers to carry the securities. If credit should not be available and the dealers had to look for buyers, that would obviously have an effect on market rates.

> Thereupon, upon motion duly made and seconded, the open market transactions during the period December 13, 1960, through January 9, 1961, were approved, ratified, and confirmed.

A staff memorandum on recent economic and financial developments had been distributed under date of January 6, 1961. With further reference to economic developments, Mr. Noyes presented the following statement:

> One business, at least, is booming--that of vivisecting the economy, diagnosing its ills, and prescribing remedies. This year the page upon page of newsprint devoted to current and prospective economic developments seems high, even after allowance for the normal seasonal peak. In these circumstances, it is difficult to say anything that does not sound like a warmed-over version of yesterday's headlines.
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> Very little that actually occurred in December can be cited as concrete evidence of a change in the down-drift that has generally characterized economic developments since last summer. Nevertheless, for reasons that are hard to pin down, there does seem to have been a slightly more optimistic tone in most economic analyses in the past few weeks, and the stock market has reflected this improved sentiment. It has also been evident in the form of less optimistic appraisals of the future course of Government securities prices.

The gross national product appears to have held about even in the fourth quarter--certainly the change from the second quarter level of $505 billion in either the third or fourth quarter is hardly significant. Industrial production was off at least a point--and probably two--in December, bringing the decline from July to around 6 per cent. Unemployment rose further to a seasonally adjusted rate of 6.8 per cent--an 8 per cent increase. Prices of sensitive materials continued to decline, and the average of all wholesale prices also drifted down a little. Steel scrap, one of the few exceptions, recovered somewhat from the very low level prevailing earlier in the winter.

The performance of department store sales, which just equalled last year's records for the Christmas season, was mildly disappointing in that it was derived from substantially expanded facilities, and sales per outlet were generally down. Total retail trade was down 1.3 per cent.

Perhaps one reason for the improved sentiment is the spreading realization, as people study the aggregate data, that so far the reductions in output are fully accounted for by shifts in inventory. In fact, final takings of goods and services have continued to increase, rising by more than $3 billion in the third quarter, and at least as much in the fourth. It is an easy step from this to the conclusion that the process of inventory liquidation may be almost complete and that, as business shifts back--first to lower rates of decumulation than the estimated $4 billion in the fourth quarter, and then to re-accumulation--conditions could improve quite rapidly.

At least one aspect of the present inventory situation suggests caution in assuming that liquidation will be reversed at an early date. Manufacturers, especially in the durable goods industries, have unquestionably liquidated a substantial amount of inventory, both of raw materials and of finished goods. There is no indication that a similar adjustment has already occurred at the retail level, however, and some signs that, in fact, inventories have continued to accumulate. Notably, we know that dealers' inventories of new cars rose slightly further in December from the already advanced November level. Production cut-backs of uncertain duration to correct this situation have already been announced. A similar, if less dramatic, situation exists in the case of other durable goods. Despite widespread price cuts and promotions, stores appear to have made little progress in reducing their stocks of hard goods or apparel in the second half of 1960. This is illustrated by the department store data, which show that stocks increased 5 per cent from May to November, compared with declines of 5 to 6 per cent in comparable periods in other postwar cycles. Thus, it appears that there is room for--and undoubtedly pressure for--a cut-back in retail stocks, which could act as a drag on

production for some time to come, even if we assume that inventory adjustment at the manufacturers' level is nearly complete.

On the other hand, even if inventory liquidation increases further, say to as much as $6 or $7 billion in the current quarter, it appears unlikely that gross national product will go much below the $500 billion mark. Without any new action, Government expenditures for goods and services will increase by at least $2 billion in the current quarter; net exports will probably be well maintained, and there is no sign of any abatement in the upward trend of personal expenditures for services, which has continued throughout the postwar period. These will more than offset increased inventory liquidation of the amount suggested, and declines from the already depressed levels of producer and consumer durable expenditures, and in construction, should not be much more than seasonal. Thus, the most plausible immediate prospect seems to be for more of the same--a very small down-drift in aggregate spending, a somewhat larger slipping off in industrial production, and a sizable further increase in unemployment. Beyond this, it is easy to fabricate assumptions which will produce either an upturn or a further decline, but there is very little factual basis for one or the other. Certainly, it is hard to find any evidence which could be said to provide sufficient basis for a dramatic shift in monetary policy at this juncture.

If this analysis of the current situation sounds vaguely familiar to those who read the report of Professor Samuelson's task force, I can only say that I started with a clean sheet of paper and a firm resolution to try to say something fresh and illuminating. The facts of the matter seem to be--to quote directly--that there is no reason for either "hasty improvisation or doctrinaire reversal of policies."

Mr. Thomas presented a factual review and analysis of recent trends and the present state of liquidity in the economy, pointing out their significance for fiscal, debt management, and monetary policies. He pointed out that, after increasing by record amounts in 1958 and 1959, the total volume of principal liquid assets held by the nonbank public increased less in 1960 than in other years of the past decade or more. There was a small decrease in the money supply and in nonbank holdings of

short-term Government securities, but a very large expansion in fixed-value redeemable assets. The ratio of total liquid asset holdings to gross national product had declined considerably in the post-war period, with but few interruptions, and in 1960 was below the previous low level recorded in 1957.

In view of this decline in liquid assets and the current state of slack in the economy, some stimulation to increasing liquidity would be appropriate. The likelihood of deficits in the Federal Government budget in the next year, necessitating an increase in the public debt, together with the large volume of Government securities maturing in each of the next five years, would provide ample opportunity for increasing liquidity through debt-management policies that permit some shortening of the average maturity. In fact, sizable longer-term issues might also need to be offered to avoid undue increases in liquidity and the creation of difficult debt-management problems for the future when less liquidity may be appropriate.

With respect to monetary policies, it was pointed out that they had been directed for some time toward fostering expansion in bank credit and the money supply. Although the response had been slow, bank liquidity had improved somewhat and during December there was an unusually large increase in bank loans and investments. The money supply increased some in December, but most of the increase recently had been in time deposits.

With reference to immediate Federal Reserve operations, Mr. Thomas suggested that the principal question was how much of the reserves

released through the remaining seasonal decline in demands for reserves should be absorbed and how much should be left as a stimulus to credit expansion. Free reserves had declined in the past week and would presumably average less than $500 million in this statement week. During the following three weeks large amounts of reserves would probably be released by seasonal decreases in required reserves and in currency in circulation, partly offset by declines in float and a continued gold outflow, as well as by a runoff of outstanding repurchase contracts at the Federal Reserve.

There could be further System sales of nearly $400 million and still leave free reserves of over $600 million while providing a level of total reserves adequate to cover normal changes in the money supply. Free reserves of over $600 million would probably give sufficient leeway and stimulus for some growth above normal, without danger of excessive ease in the money market.

Mr. Marget presented the following statement with respect to the balance of payments and related matters:

> I regret to report that, since my last report to this Committee on October 25, there has been a development with respect to gold outflow which is disquieting. The reason for this is not only, or even primarily, the level of the gold outflow. That level has, to be sure, become uncomfortably high since October: from an October level of $280 million, which was bad enough, gold outflow rose in November to $490 million, and in December (if we leave out the special sale of $300 million in gold to the United States by the International Monetary Fund) it was $440 million. For the first week in January, the figure was also very high: $130 million.

What is disquieting about this is not the mere fact of the large increase in the rate of outflow, but the nature of the forces lying behind this increase. Up to last November, it was possible to say that, despite our balance-of-payments difficulties, there was no evidence of a "flight from the dollar," in the sense of a significant conversion of dollar balances by the holders of those balances into gold. Our proof of this was the level of those dollar balances themselves. As long as these dollar balances not only failed to show any significant decrease, but actually continued to increase, it was impossible to argue that a "run" on the dollar was occurring.

But the situation in this respect changed suddenly in November. After an increase in foreign liquid dollar holdings in October of $160 million, these holdings in November showed a decrease of $470 million. We do not yet have the complete data on foreign liquid dollar holdings for December. But what we do have is information indicating beyond question that a number of foreign monetary authorities which up to now have refrained even (unlike a country such as Great Britain, for example) from converting into gold new accretions of dollars, are not only converting, or are planning to convert, such new accretions of dollars into gold but have been converting, or are planning to convert, a considerable portion of their existing dollar holdings into gold.

I do not wish to seem unnecessarily alarmist about this. For one thing, in some cases--those of Peru and Argentina, for example--the increase in the ratio of gold holdings to dollar holdings does represent a reversion to practices followed by these countries over extensive periods in the past. For another thing, even a country's announced intention to convert into gold may be subject to change, or at least to a rate of implementation which would not create serious difficulties for us. There is the case of Japan, for example, which up to now has been content to retain its dollar holdings instead of converting them into gold. On December 20, the Japanese Finance Minister, in reply to an interpellation in Parliament, stated that the Government of Japan wished to increase the ratio of gold in Japan's reserves from the present 14 per cent to 30 per cent "following the example of other countries." This would mean, in the case of Japan alone, an increase in gold purchases of $350 million above what would have been expected on the basis of balance of payments considerations alone. The Minister added, however, that he was "in no hurry to purchase gold right now"; and we have had subsequent communications indicating that there is a strong element among the Japanese which is vigorously

opposing the indicated change in gold policy and is proposing that if, for internal political reasons, the Japanese Government feels it necessary to convert some of its dollar holdings into gold, it should do so only at a rate not exceeding, say, $10 million a month.

But if one should not be unnecessarily alarmist about this new development with respect to gold outflow, neither can one afford to be complacent about it. There can be no doubt that we are now confronted by a new development. It is, moreover, the kind of development which could very easily, and very quickly, feed on itself, in precisely the way in which a run on a bank can feed on itself. There is no use looking off in another direction and saying that this could not possibly happen, when in fact it may be happening under our very eyes.

It is one of the paradoxes of the current situation that nothing has happened with respect to our basic balance-of-payments position which would warrant a sudden loss of confidence in the dollar on the part of foreign monetary authorities. On the contrary, it can be argued (as it is in fact argued on page 26 of the current staff report on recent economic developments prepared for this Committee) that, at the very time when the gold drain has been accelerating, our deficit on current and long-term capital transactions combined (leaving out of account, that is, only short-term capital movements, which by definition may be regarded as reversible) was running at a seasonally adjusted annual rate of under $1 billion. We have to keep on reminding ourselves, to be sure, that this improvement in our basic position, which owes so much to the improvement in our exports that brought our trade surplus to a seasonally adjusted annual rate of around $6 billion in October-November, has greatly profited from the favorable cyclical constellation that has been prevailing as between the United States and its principal trading partners. But the fact remains that we have been able to effect this improvement in our basic international position by means of a basically "liberal" commercial and financial policy, while maintaining, at the same time, a very considerable degree of flexibility in our domestic monetary policy; and we have been able to do this because of the strength of our reserve position in terms of gold. It would be a very serious matter indeed if both the liberal foundations of our international commercial and financial policies for bringing our international accounts into balance and the degree of flexibility which we have been able to maintain in our domestic monetary policy were to be shaken by so rapid a deterioration in our reserve position,

as the result of gold losses due to a loss of international confidence in the future of the dollar, that we should have no alternative to a policy of contraction, on both the international and domestic fronts, which would be the very opposite of what may be called for by the basic economic facts of both the international and the domestic situations.

The heart of the current problem, then, is the restoration and maintenance of that international confidence in the dollar which, if the evidence that has been accumulating since October in the field of gold movements is to be taken as a portent, has begun to be shaken. It is not for me to undertake to specify all the elements that may have entered into the pessimistic appraisals with respect to the future of the dollar that obviously underlie these new developments in the matter of gold movements. Since, however, there are some voices (very much in the minority, I must say) which do not exempt Federal Reserve policy from bearing a part of the responsibility, I should like to quote what has been said recently on this matter by the Managing Director of the International Monetary Fund, Mr. Per Jacobsson, who is in as close touch with the sentiment of foreign monetary authorities as anybody, and who has gone very much further than most observers in attributing our balance-of-payments troubles to the internal financial policies -- specifically the fiscal policy -- pursued in 1958:

> "I would say, for my part," he declared in a speech delivered on November 17, "that the easing of credit conditions recently undertaken by the Federal Reserve System has been the proper policy . . . . In view of the sharp increase of exports over imports of merchandise, it seems to me that balance of payments considerations ought not to stand in the way of the proper measures which should be taken for internal reasons, especially as the transition from an inflationary psychology to the expectation of more stable prices will insure greater attention to costs." And again on December 13 last: "I think that, in the present state of activity, the authorities can well permit the continuation of fairly easy money, and also take steps to stimulate activity, especially in the depressed areas, provided the measures taken do not lead to cost increases or hamper the essential adjustments of the free market."

The proviso, quite obviously, is of very great importance indeed; and there is hardly likely to be dissent from it in principle from any quarter. But what will be watched, in the

weeks ahead of us, will be not so much formal statements of principle as the policy actions actually undertaken. The nature of the gold movements that have been under way since October is a vivid reminder of what can happen if the policy actions undertaken by the United States in the immediate future are such as to undermine, instead of strengthening, foreign appraisals of the future of the dollar. We can ignore that reminder only at our peril.

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

Economic activity continues its sluggish course. So far, there are no signs of snowballing downward momentum. Nor is there evidence of a revival near at hand. A further contraction of modest proportions seems the most likely near-term course.

The greatest downward factor has been the shift from inventory accumulation to inventory liquidation. Final demands have held up fairly well, receding a bit in the case of business and consumer demands but rising in the case of Government and net export demands.

To date, the downturn has been milder than in comparable periods of other postwar recessions. Unless business sentiment and consumer sentiment take a decided turn for the worse, there is a good possibility of an upturn by midyear. However, even if such an upturn does develop, there remains the important question as to the vigor of the upturn and its ability to make significant inroads into our idle manpower and productive capacity.

Changes in the fiscal situation of the Federal Government are already having some effect on the business outlook. Government income has been less than that estimated earlier in the year. It now looks as if there will be a modest cash deficit for the fiscal year ended June 30, 1961, whereas the official estimates made twelve months ago indicated a budgetary surplus of several billion dollars. The latest projections do not take into account any increase in spending or reduction in taxes that may possibly be voted by the new Congress.

Bank credit in December showed a strong rise. Much of it, however, was caused by heavy borrowing by Government securities dealers and finance companies as well as by business concerns around the mid-December tax and dividend dates. There has been some evidence recently of modest bank purchases of intermediate-term Treasury issues.

December was marked by a moderate easing of congestion and strengthening of prices in the long-term capital markets. So far, bank purchases of longer-term securities have been on too modest a scale to have had any great effect in reducing long-term rates, but if such purchases continue they could develop into an important factor tending to reduce long-term rates. In general, however, an attitude of caution pervades the bond markets.

The balance-of-payments situation continues to be highly sensitive. The amount of United States exports in November was gratifying. We continue, however, to lose gold. The loss of gold in November was offset considerably by a reduction that month in foreign liquid dollar holdings in the United States, suggesting that the over-all balance of payments may be coming into better balance.

The recent declines in short-term rates in some financial centers abroad have been helpful to us. It seems reasonable to assume that the decline in interest rates abroad has been a factor in the tapering off of the outflow of short-term United States funds. Yet the rate gap remains wide enough so that we cannot relax our concern about any downward pressure on our own short-term rates.

The recent heightening of tensions in various parts of the world, and the approaching change-over in our own national Administration, add further to the sensitivity of the current situation. Thus, it is highly important that everyone concerned with our country's financial policies show a determination to preserve the soundness of the dollar.

We think that the domestic economic situation calls for a continuation of the current policy of credit ease, but that it is of overriding importance to avoid any substantial decline in short-term interest rates, particularly the rate with respect to three-month Treasury bills. Such a reduction would tend to encourage the transfer of short-term funds to foreign markets and thereby worsen our balance-of-payments problem.

We think it would be unwise to change the discount rate and that there is no need to change the directive. We think it desirable to seek to maintain about the same degree of ease as has existed in the period since the last meeting of the Committee. The feel of the market as to the degree of ease is more important than the level of free reserves. For example, it would seem more meaningful to aim at a sufficient supply of reserves so that Federal funds are usually available somewhat under the discount rate.

The problem of promoting monetary expansion while avoiding a downward pressure on short-term rates is a difficult one. Long-term rates are most important for investment spending; short-term rates are most important for foreign balances. We must continually strive for a flexible policy that will serve best our various interrelated goals. To this end, it may become desirable for the System to sell short-term securities and to buy securities of other maturities that are in supply in the market. I am not suggesting that we undertake such a program between now and the next meeting, but I do suggest that all of us continue to study the ways in which our practices can best meet the new problems confronting us.

Mr. Erickson reported that on balance economic activity in the First District continued to reflect the easing tendencies that had been evident in recent months. The New England production index was up one point in November to 116, but it was still three points below the previous year. Except for the General Electric strike, the index might well have been higher in October than in November. The December survey of New England purchasing agents was markedly poorer than other recent surveys of that group. Electric output, however, reached new highs in the weeks ended December 17 and December 24. In November, nonagricultural employment was slightly lower than in the previous month, and the figure was only .1 of one per cent higher than in November 1959. Insured unemployment was still running more than 30 per cent in excess of the previous year. Turning to construction, however, the picture was brighter. Awards in November were 24 per cent ahead of November 1959, following an increase of 11 per cent in October. For the first 11 months of the year, awards were down 4 per cent from the previous year, reflecting a substantial

reduction in awards for public works and utilities. Nonresidential construction was up 14 per cent and residential construction was down 4 per cent, the latter figure being much less than the national average. As to retail trade, business for the Christmas season was 3 per cent higher than in 1959. Although two more shopping days were included this year, these were offset by a blizzard which lasted more than two days. For the year, the District finished 2 per cent higher than in 1959, which was better than the national average. Automobile registrations were still running well ahead of year-ago figures.

Mr. Erickson went on to say that as of December 28 weekly reporting banks in the District showed an increase in commercial loans of about the same proportions as nationally. In the past four weeks District banks were sellers of Federal funds more often than they were buyers. The discount window was used very little.

Mr. Erickson said that in view of the national situation and the international situation he would make no change in the discount rate or in the directive. He suggested that the instructions to the Desk be about the same as those given at the previous Committee meeting, which would envisage an easy situation but not excessive ease. He hoped that Federal funds would sell under the discount rate and that the short-term Treasury bill rate would remain somewhere around the present level.

Mr. Irons reported that there had been no particularly significant developments in the Eleventh District. Conditions were continuing to

follow about the same trend that the District had been experiencing, both in terms of comparisons with the preceding month and in comparison with national figures. Most of the movements were within a range of 1 to 2 per cent from the preceding month or from year-ago figures. Christmas trade was good, better than people thought it would be in the first week or two in December, but almost any statistical comparisons could be presented depending on the definition of the length of the Christmas season. Employment had shaded off a bit in the past month, and unemployment was up a little, with about 5 per cent of the labor force unemployed in December. The petroleum situation had shown some slight improvement. In general, the economy was moving along about as it had been, with perhaps a very slight trend downward but nothing startling in any area of activity.

Turning to banking, Mr. Irons said the situation was clearly easy. Loans, investments, and deposits rose rather substantially in the past month, and when the call report figures had been added up he thought they would be appreciably above the previous year. As was true nationally, there had been a substantial increase in time deposits. Borrowings from the Reserve Bank during December and early January were negligible. District banks had been net sellers of Federal funds, with net sales larger than during the preceding month.

Mr. Irons said he supposed, in view of economic conditions, that it would be appropriate to continue to follow a policy of ease and to be

sure that reserves were adequate to enable the banking system to meet any reasonable requirements imposed upon it. This situation appeared to have prevailed during the past 3 or 4 weeks, and he would suggest continuing the present policy, although perhaps a little less aggressively. He would think twice before deviating on the side of ease, and it would be his preference to maintain free reserves in the area of $500-$600 million rather than $600-$700 million. He shared the apprehensions expressed by Messrs. Marget and Treiber regarding the international situation. The time might be getting nearer when more consideration would have to be given to that problem and there would have to be a shift in the direction of policy to narrow the rate differential, but he did not think that such a point was yet at hand. He would like to see the bill rate more in a range from 2-1/4 to 2-1/2 per cent, preferably the upper part of that range. The Federal funds rate should be below the discount rate, but not much below.

In summary, Mr. Irons said, he would try to avoid aggressively pushing reserves into the market. The domestic situation called for a policy of ease, but not a policy of very aggressive ease, especially when tied to an international problem which continued to discourage him more than the domestic situation. He would not favor a reduction of the discount rate. In fact, he could almost find arguments for an increase, although he was not at the point of making such a proposal at the moment. He saw no reason for a change in the directive.

Mr. Mangels reported that the over-all business picture in the Twelfth District had not changed much in recent weeks. A substantial pickup in department store sales during the last two weeks in December was sufficient to offset somewhat depressed conditions in the first part of the month, with the result that sales figures for the five-week period ending December 31 were about 3 per cent better than the previous year. Automobile sales in California for the first week in December showed a 25 per cent increase over the daily average in November, and the November figures were about 11 per cent higher than in the same month of the previous year. Steel production, at a little over 50 per cent of capacity, was better than the national average. In November, total construction was about 7 per cent above the figure for the previous year, most of the increase being accounted for by public works and utility contracts. On the darker side, lumber production reached a new low in November, and orders in that month were lower than for any other month of 1960 except January. Unemployment in the Pacific Coast States in November was at the rate of 6.6 per cent; this figure reflected a slight improvement from 6.8 per cent in October, but it was the highest November rate for the past 11 years. On the other hand, civilian employment in Pacific Coast States was at an all-time high level in November.

Mr. Mangels said that demand deposits of District banks had increased somewhat and that time deposits were up considerably, with a rather substantial increase in savings deposits, in December. Total bank credit showed the

largest increase of the current year in December, with loans up more than $200 million and Government securities holdings up more than $250 million. In the past week or so, sales of Federal funds by District banks were about double the amount of purchases. The December interest rate survey of short-term business loans showed an average rate of 5.31 per cent, compared to 5.4 per cent in September and 5.57 per cent in December 1959. About one-third of the dollar amount of the loans covered by the survey were made at the prime rate of 4-1/2 per cent, as against one-fourth in September, but the rate reductions were confined largely to loans in excess of $100,000. There had been practically no borrowing at the discount window.

Mr. Mangels recalled that it was mentioned at the December Committee meeting, and again today by Mr. Thomas, that loan-deposit ratios of banks continued to be high. He noted that the average for New York City banks in December was 68.1 per cent, against 68.6 per cent in November, while outside of New York City the average was 59.5 per cent compared with 61.2 per cent in November. Over the past few months the decline of ratios had been small, and banks therefore probably were not looking aggressively for increases in their loan portfolios. Under these circumstances, and in order to provide a slightly greater degree of ease, it would be his thought that the Desk should absorb less than the amount of reserves that would become available in the forthcoming period. He would try to maintain an easy tone in the market and to keep net free reserves in the range of $600-$700 million. The present directive seemed

satisfactory, particularly in its reference to the international situation, and there seemed to him to be no need to change the discount rate.

Mr. Allen said that in the Seventh District a slow, gradual decline in economic activity seemed to have continued. Official employment data available through November showed reduction in virtually all lines of manufacturing, and fragmentary data available from other sources indicated that the trend had continued. Further reduction of automobile production schedules meant that unemployment would increase in January, particularly in Michigan.

Automobile production schedules for January called for 489,000 units, Mr. Allen reported, although private estimates were 450,000 or less. That would compare with 522,000 produced in December. Car production of 6,700,000 in the year 1960 represented the second best year in history, but saleswise the total of 6,143,000 cars was the third best year. Opinions obtained by the Detroit Branch suggested that 1961 sales might fall to 5,600,000. Although others in Detroit were more optimistic, it seemed rather certain, in the light of substantial inventories, that 1961 production would be well below that of 1960, which did not brighten the employment outlook.

Department store sales in the Seventh District showed a gain of 3 per cent over 1959 in the four weeks ended December 31. In the last week of the year the new index of steel production was 75 in Chicago and 68 in Detroit, compared with 59 for the nation. Three mail order houses

had announced that their spring and summer catalogs contained price cuts, one stating that its prices averaged 2.4 per cent below last year and were the lowest since 1955. Farm income in the District in 1960 was substantially higher than in 1959, and it appeared that 1961 income would be close to that of 1960.

Mr. Allen went on to say that the use of bank credit by business remained below normal. At District weekly reporting banks, loans to commercial and industrial borrowers in December were down $60 million, the first time since 1957 that these banks had reported a reduction in business loans in the last month of the year. Deposits by reporting banks, both demand and time, rose in December; this had been the case for smaller banks throughout the last half of the year. Data on bank reserves and borrowing indicated that reserve availability was still quite large.

Mr. Allen commented that the picture in the Seventh District, which he had attempted to summarize, was a mixed one. Certainly there were favorable as well as unfavorable factors. Reserve availability, the particular concern of the System, seemed adequate at this time to support a substantial increase in bank credit.

For the time being, Mr. Allen said, he failed to see that a change in monetary policy was called for or would contribute to an improvement in economic activity. Therefore, he would not advocate changes in the discount rate, the directive, or the degree of ease.

Mr. Leedy said that because of the importance of the winter wheat crop in the Tenth District the condition of the growing wheat exerts a psychological effect over a widespread area. The December report showed that the condition of the wheat was from good to excellent, although 1961 production was estimated at about 12 per cent less than the very large crop harvested in 1960. Snow and cold weather had slowed the use of wheat pasture in parts of the District, but generally there was adequate grazing for cattle and sheep. Because of abundant feed supplies, a considerable number of livestock had been withheld from the market. Also, some sales of livestock, as well as last year's crops, had been deferred to the current year for tax purposes, and as a result cash receipts from farm marketings in District States during the fall months were below the previous year. Seasonally adjusted nonfarm employment was unchanged from October to November, the latest month for which figures were available. Following the trend that existed throughout most of 1960, there was a slight decline in manufacturing employment, but this was offset by a rise in nonmanufacturing employment. The cutbacks in defense contracts to the aviation industry were a factor contributing to the lower level of manufacturing employment. Apparently there would be some further decline in manufacturing employment in the early part of this year due to layoffs that had been announced by automobile company assembly plants. The volume of construction was lower during the first 11 months of 1960; the figures for December were not yet available. While increases in construction

contracts started after July, these were mainly due to nonresidential contracts and to the continued high level in the public works segment. In December there was a significant increase in department store sales which continued through the end of the year, with the result that the year wound up on the plus side, although only by about 1 per cent.

Turning to the banking developments in the District, Mr. Leedy said that loan demands failed to suggest any great strength in the business segment during December. However, reporting member banks did increase substantially their portfolios of Government securities in the maturity range of less than five years. At the end of the year total deposits of reporting member banks were about $170 million higher than at the end of 1959, with more than half of the increase -- around $94 million -- in time deposits.

As to policy, Mr. Leedy said it seemed to him that in the period until the next meeting the Committee should undertake to see that further easing in reserve positions did not occur. Although the statistics did not seem to lend much support to the optimistic psychology which appeared to have developed quite recently, nevertheless that was a factor that could not be ignored. As long as the Federal funds rate was moderately below the discount rate, and as long as the bill rate fluctuated in a range as high as 2-1/2 per cent, he would not be too much concerned. Apparently there was going to be a chore of absorbing reserves, and he would prefer to make sure that the System absorbed enough rather than

to operate in the other direction. He would not make any further change so far as System action was concerned.

Mr. Leach reported that in the closing weeks of 1960 business activity in the Fifth District was marked by small but general and widespread declines, with only a few elements of strength and stability. Both employment and man-hours in manufacturing, seasonally adjusted, were down in November and reached their lowest points of the year. Demand for textile products was still slow and the mills remained on shortened schedules. Inventories continued to accumulate and backlogs had dwindled, while prices had eased further and were down substantially from a year ago. New orders for lumber had continued to lag behind production and shipments, and extended holidays were scheduled to keep output closer to demand. Bituminous coal production during the first half of December was 25 per cent below the comparable period a year earlier even though foreign shipments were higher. The few elements of strength and stability included the following: Employment in construction had been steady for the past six months at a level somewhat above that of a year earlier. Contract awards for residential construction in November indicated that activity in that area might be turning up after a long decline. Employment in the fields of finance, services, and Government had been steady or rising slightly. Cash receipts from farming in the District for the year 1960 were up 7 per cent from 1959 due to higher yields on smaller acreage and better prices, with most of the gain occurring in tobacco, the marketing season for which ended in December.

The position of District member banks had eased further, Mr. Leach said. Since the Committee meeting in December, business loans of weekly reporting banks had expanded less than seasonally, and total investments had continued their contraseasonal rise. The increase in investments since the end of August had now reached nearly 11 per cent, well above the rise during any recent year, with most of the increase occurring in Government securities maturing in less than one year. Borrowings at the discount window had averaged only $2.5 million the past four weeks, less than for any four-week period since 1952. District banks remained large net sellers of Federal funds.

With respect to policy, Mr. Leach said he continued to believe that easing actions taken by the System since the decline in business activity began last spring had been timely and sufficient. Monetary policy seemed to him to have already made its full contribution, barring a greater deterioration in economic conditions than now appeared likely. In view of the sizable expansion in time deposits, he was not as much concerned as some appeared to be about the failure of the money supply to expand more rapidly. Banks should not be expected to make loans in the absence of legitimate loan demand, and apparently under existing conditions substantial amounts of demand deposits were being transferred into time deposits because of unwillingness of the holders to spend. During the past year the seasonally adjusted money supply decreased 0.9 per cent while time deposits were rising 8.2 per cent. Of course, there

are sound reasons for excluding time deposits from the definition of the money supply, but one should not lose sight of the fact that the money supply plus time deposits increased by 2 per cent while the money supply itself was decreasing 0.9 per cent.

For the forthcoming period, Mr. Leach indicated that he would favor maintaining substantially the same degree of ease as in recent weeks, taking care to mop up the reserves that appeared because of seasonal reasons so as to avoid greater ease and a decline in short-term rates. He saw nothing to be gained by lower short-term rates, and something could be lost. He would be opposed to any lowering of the discount rate at this time, and he saw no reason to change the directive.

Mr. Mills commented that over the period of each calendar year the deliberations of the Open Market Committee shift their focus from one economic and financial area to another, but inevitably decision-making is tied to the interpretation of statistics that represent past events. On occasions, therefore, decision-making will lag behind the events that are rushing to a conclusion. Mr. Marget's cogent discussion of the balance-of-payments problem was based on events that had occurred recently and were occurring currently, and they suggested that the focus of the Committee's thinking and policy-making should shift drastically from the domestic scene to the international scene. The interpretation that he (Mr. Mills) would place on policy thinking in recent times was that it represented in effect an attempt to poultice over cracks in the domestic economy through the application of a monetary policy of ease at

a time when it was quite probable that the cyclical trend of events could not be responsive to monetary policy. An evidence of that fact was the situation which found the rate for Federal funds running consistently below the discount rate, which would signify to him that funds were piling up in the money market centers and were not being put to employment by the recipient banks for reasons that had been repeatedly expressed, most recently by Mr. Irons. Looking strictly at the domestic scene, there seemed to be little reason to follow a policy of continued monetary ease or to attempt to maintain a level of net free reserves that was futilely ignoring the responsibility on the part of the banks to expand the resources placed at their disposal. In his view, it would be much more in order to permit the reserve positions of the banks to tighten to a degree that would find the short-term interest rate moving up from its present artificially low level to a more realistic level which would be conducive to checking the outflow of funds and possibly reversing it.

Mr. Mills commented that his own approach was a more heterodox one than that of Mr. Irons. The latter's approach dealt with the situation more gingerly, whereas in Mr. Mills' view the economic affairs of the country had reached a point where it became necessary to use monetary policy as a surgical scalpel to correct dramatically a very difficult international financial situation. He would not go into the means by which he would apply that scalpel because a sensitive area was involved that deeply concerned the Treasury, but he wished to call to the Committee's

attention that in the press yesterday and this morning there were notices that the President-elect was calling today on the Secretary of the Treasury. He also called attention to the fact that the New York Chamber of Commerce, a responsible body, had issued a statement of its concern about the international financial climate. The point he was leading up to was that it was a serious responsibility of the Federal Reserve Banks and of the members of the Board of Governors to take into account first the international situation and to consider what definite steps should be taken that would be most conducive to a more harmonious international financial picture.

Mr. Robertson said that he too was concerned about the remarks that had been made this morning concerning the international situation, especially to the extent that they touched upon diminution of confidence in the stability of the dollar. It seemed to him that the major contribution the Open Market Committee could make today toward increasing the confidence of the world in the stability of the dollar would be to follow a policy that would do whatever was possible to reverse the trend of the economy in this country. The failure of bank lending rates to go down was an indication that the System had not moved fast enough or far enough, and the same thing was true with respect to long-term rates. Consequently, he would favor moving toward a greater degree of ease than yet achieved. He would be much more reluctant to absorb reserves that would come into the market over the next few weeks than others around the table had

indicated; he would favor permitting a greater abundance of reserve availability in the hope that this would have an effect in reversing the economic trend. This, he felt, was the real way in which System policy could be effective. If the System adhered to what he regarded as the short-sighted view of over-emphasizing the short-term Treasury bill rate because of the international situation and the outflow of funds, that outflow might in fact be prolonged. In his opinion, it would be much better to let the bill rate go lower and turn the economic picture around. He also would indicate to the world the position of the Board of Governors and of the Federal Reserve System by reducing the discount rate.

Continuing, Mr. Robertson said that since this was the beginning of a new year he wished to express the hope, first, that in 1961 the Desk would adhere to the rulings of the Committee, until they were changed, regarding the use of repurchase agreements at lower than the discount rate by using such agreements sparingly rather than at every opportunity. Second, he hoped the Desk would refrain from offsetting every temporary fluctuation in float merely to maintain a statistical free reserve figure. The result of attempting to offset those fluctuations was not to change the economic picture or the effective reserve structure of the country but merely to subsidize the dealers who profit from the handling of purchase and sale transactions.

Mr. Robertson said he saw no reason to change the policy directive which, in its present wording, could be implemented in the manner he had suggested. In fact, the directive appeared to call for such a policy.

Mr. Shepardson said it seemed to him the economy of the country was facing a situation that it had been due to face for a considerable period of time. It was beginning to be realized that there is a difference between a seller's market, such as had existed for about twenty years, and a buyer's market which is the constructive type of marked for a healthy sustained growth of the economy. While some of the adjustments were painful, nevertheless wholesome adjustments were taking place.

With reference to the considerable amount of current discussion regarding depressed areas and the relief needed for them, Mr. Shepardson related a report that had come to his attention regarding the situation in the Wheeling, West Virginia, area where a group of labor people had decided that jobs at reasonable wages were better than no jobs at exorbitant wages and had started to try to rebuild industrial activity through positive action to assure stability of the labor force. While this was only a single incident, it seemed to him that the publicity it was receiving was wholesome. He did not believe that flooding the market with money at this time to try to stimulate loans which borrowers and lenders obviously did not consider desirable would do any good. Instead, it seemed to him that a posture of not constituting a restraining influence represented as much as the System could do to assist the domestic economy. In addition, the international situation was of increasing importance. For these reasons he aligned himself with those who would not favor further ease. As a matter of fact, he would be inclined to go along with the view that somewhat less ease than now prevailed might be appropriate.

It seemed to him that this was not a time to change the discount rate and that there was no need to change the directive.

Mr. King said he had little faith in the ability of monetary policy to reverse the present economic trend. He believed that business was awaiting the actions of the new Administration and the new Congress, and this view had been strengthened in recent conversations with knowledgeable members of the business community. Businessmen were watching the situation carefully and the domestic economic trend would be based largely on the decisions that were made. Internationally, people also would be watching the new Congress and the new Administration closely. Mr. King went on to say that he had frequently scoffed at pessimists and had watched them turn out to be wrong. However, he believed that a point had been reached where it would be a dangerous course to be optimistic and to be wrong. In his own view, and on the basis of comments by people with whom he had talked, this year would probably be a year of drifting--some might call it sliding--during which some contradictory indicators would be seen. Activity might start up for a while and then slow down in some sector of the economy, while activity in another sector might go down and then level off. Frankly, he was concerned. He did not feel that there could be any decisive movement upward, for the factors that would make such a movement possible did not appear to be present. The operating budgets of business concerns were being cut, in some instances with which he was familiar, and profit margins were expected to be lower than in 1960. It appeared to him that an era had been entered in which it would be

necessary to learn to live without inflation. A restraint was imposed automatically by international conditions, and it probably would have arisen at about this point regardless of monetary policy. In his opinion this was a time when the System ought to be willing to explore all avenues as objectively as possible. It was a time to overcome lethargy and to explore, at least, any new avenues without formulating conclusions in advance.

Mr. King expressed the view that the money market should continue to have a feel of relative ease. He wished to align himself with the views of Messrs. Irons, Mills, and Shepardson and of others who had spoken in the same vein. One of the things that would be needed in the year ahead was statesmanship on the part of commercial bankers, and he hoped that this quality would be found. He hoped that it would be possible to have some improvement in longer-term rates, but that seemed to lie within the province of the commercial banks. If there should be some improvement, the System might undertake a reinforcing effect to assure, to the extent possible, that the bill rate did not recede from its present level and, as time went on, that the rate worked into somewhat higher ground. Although he did not believe it was feasible to ask the Desk to aim at any particular level, he hoped that over the forthcoming period the trend could be upward. If there was to be any change in the discount rate, he was inclined to feel that it should be upward. An increase might not do

any great harm, but it would tend to deter any improvement that might be hoped for in the longer-term rates of the commercial banks. Therefore, he would leave the discount rate unchanged. He supposed that free reserves probably would fluctuate fairly widely, but he would leave operations to be guided principally by the feel of the market, keeping a tone of relative ease. In his opinion the availability of more money was not going to solve the present dilemma.

Basically, Mr. King said, the pendulum had swung over the years from a position of too much power on the one hand to a position of too much power on the other hand. Specifically, he had in mind increases in wages which were artificial because they did not recognize any real increase in output. For the Government at this time to indicate to businessmen and particularly to world bankers that it still thought it could legislate prices would be an unfortunate situation. He realized that he had just talked about influencing the bill rate to move in a certain direction. In fact, however, the System does operate in the bill market; the purposes of the Federal Reserve call for operating in that field. Therefore, he did not feel that any contradiction was necessarily involved.

Mr. Fulton said that most Fourth District business barometers had sagged to their lowest points of 1960 at the end of the year. The sluggishness of automobile sales possibly was due to bad weather toward the end of the year; for the year as a whole, sales were 8 per cent above 1959.

Department store sales barely measured up to the 1959 total for Christmas season, although sales for the year were about 2 per cent ahead of the previous year. Construction had held up fairly well throughout the year, with the strength largely in the commercial sector. For heavy industries, the picture was far from bright. Steel orders thus far in January were about 5 per cent above December, but that month was marked by the closing of the mills over a long holiday, with the result that December was an extremely low period. Although some orders were coming in to fill low inventories, by and large the situation was very spotty. The automobile companies were cutting back on orders now on their books and were deferring deliveries. Furthermore, foreign steel was now beginning to come in in greater quantity and at lower prices. If foreign economies turned down and steel production was not fully used, United States producers expected that there would be cut-rate competition in greater volume. Wages also were a problem. There had been one wage increase in December, according to contract, and another was due next October. This would increase costs to the extent that a price rise seemed inevitable, which in turn would further weaken the competitive position of the industry.

Mr. Fulton then commented briefly on a talk given in Cleveland last night by Mr. Per Jacobsson, Managing Director of the International Monetary Fund, who emphasized the relationship between costs of American and European producers. Mr. Jacobsson said in effect that if the cost of

United States goods was watched closely, the competitive situation would to a great degree take care of itself. United States producers must be realistic about their costs, and the elements going into them would have to be controlled carefully.

In further comments on the steel situation, Mr. Fulton said that the outlook for this year was not too good. It was expected that production would be about the same as in 1960, that is, approximately 100 million tons, with some hope that by the fourth quarter production might get up to an annual rate of about 120 million tons. Producers were faced with the fact that modern mills had now been erected throughout the world with United States funds. These mills would be operating with low-cost labor, but they would be turning out good steel. Moreover, less steel was being used per unit in the manufacture of automobiles and appliances.

With reference to the new index of steel production, Mr. Fulton noted that the index used 1957-59 as a base period. There was a recession in 1958 and a long strike in 1959, so the base figure was only about 97 million tons a year, or about 1.86 million tons a week, compared with actual capacity of about 150 million tons per year at present. Therefore, although a national average of 73.1 for the latest week would at first seem to reflect a fairly good situation, in fact production was very low.

As to the foundries, which are regarded as a good indicator of the future, Mr. Fulton said he had been told that the trend of production

could be called sideways, but only because it could not get much lower. Again, foreign competition was part of the picture. Some materials could be laid down in Chicago via the St. Lawrence Seaway for a lower price than the foundries in Chicago could make them.

The unemployment situation in the Fourth District was getting worse, Mr. Fulton said. Nine major labor market areas were now classified as having a substantial labor surplus as against six in July. The latest available report did not include Cleveland, which by now was undoubtedly in that category. In a recent survey of employers, 40 per cent of the respondents expressed the opinion that there would be no change in employment in the first quarter, 30 per cent expected a decline, and only 14 per cent expected improvement. The layoffs in the auto industry had affected the District directly because of the many parts made in Ohio and Pennsylvania.

Summarizing, Mr. Fulton said that the Fourth District outlook was not good. Nevertheless, he wished to associate himself with the view of Messrs. Mills and Shepardson that an increase in ease would do nothing for the economy except to make money rates sloppy, a situation that in his opinion would not be desirable at this time. It would not encourage banks to lend; their high loan totals were the factor that established their policy. Neither would increased ease encourage people to buy. Accordingly, he felt that this was a time to hold steady, with about the same degree of ease, or a slightly firmer tone, in order to protect a bill rate of approximately 2-1/4 to 2-1/2 per cent. He would not recommend any change in the discount rate or in the directive.

Mr. Bopp said there was nothing in the Third District to give cause for much hope. The unemployment situation was particularly disturbing; since last spring new and continued claims for unemployment compensation had risen steadily, and they exceeded the high level reached in 1958. However, spending, although showing sluggishness, had held up fairly well. A late spurt brought department store sales for the Christmas season to a level 2 per cent above 1959; for the year as a whole, sales were about even with 1959. District banks had been experiencing increases in loans and investments and in deposits recently, and their reserve positions were reasonably comfortable.

Mr. Bopp indicated that he would not favor a change in the directive or in the discount rate. As to open market operations, he would recommend continuing along essentially the same lines. He was hopeful that the Federal funds rate would be consistently below the discount rate and that the bill rate would stay at about the level presently prevailing.

With respect to the longer run, Mr. Bopp commented that the ease that had been achieved did not seem to have permeated the markets as much as one would like, particularly the longer-term market, and at times the money centers outside of New York seemed to experience considerable tightness. In 1954 and 1958 the System reacted to similar developments by flooding the market with funds, hoping that if sufficient funds were injected they would slop over to the long-term market. There had been some second thoughts on that policy. However, the present situation did raise the

question whether it might not be possible to be somewhat selective in putting funds into the market. Possibly, for example, reserves might be provided at an appropriate time by a reduction of reserve requirements for central reserve and reserve city banks rather than entirely by the purchase of bills. Diverse developments in the long-term market and in some areas of the country during a period when generally easy conditions prevailed led one to wonder whether something could not be done in the areas where one would like to see something happen.

Mr. Bryan said that in the Sixth District nothing dramatic was happening in the economic field. The figures still showed a slow, steady deterioration. None of them seemed to be worsening significantly, but most of them were deteriorating a little more than the comparable national figures. In the nation, as in the District, a slow deterioration seemed to be in process. It could be argued on a variety of hypotheses that the economy was nearing a turn-around, but this remained hypothetical and at present one must face the fact of deterioration. One could also argue on a variety of other hypotheses that the economy was going to slide faster.

Continuing, Mr. Bryan said he had been reviewing System policy over the past year and, in the light of that review, trying to make up his mind what the System ought to do. It seemed that there had been several significant developments in the past year. The System had largely gotten the commercial banks out of debt, there was now a practical minimum of borrowing, and the banks had built up their excess reserve position.

There had been a rather dramatic shift in free reserves from the beginning of the year to the present time, and since mid-year total reserves had gone up rather dramatically. In his opinion, that was all to the good and the System had not gone too far. On the other hand, while he had made a number of criticisms in the early part of the year, he could not find any essential criticism in what had been done over the year as a whole, particularly in the second half.

Mr. Bryan said he had again taken a look at the longer-run situation in respect to reserves. Unadjusted reserves were just a little above the long-run 3 per cent trend line, and on a seasonally adjusted basis reserves were not significantly below the line. Therefore, he found himself reasonably satisfied with the System's posture at the present time and he had the feeling that nothing dramatic needed to be done. The policy he would advocate was one of "staying where we are" and very slowly and very modestly adding a little to the reserve supply to permit the banks to provide for the normal and natural growth factor that is necessary in the economy. In this connection, Mr. Bryan referred to a staff memorandum, distributed under date of January 9, 1961, presenting tables designed to provide the Committee a set of data that might serve as a test of past performance and a guide to operations in the immediate future. For the next three weeks, he said, he would be delighted if the figures could be attained that had been projected, although he would add to those reserves something very modest, perhaps $50 million, as a growth factor.

Turning to the international situation and the balance of payments, Mr. Bryan said he shared the feelings of alarm that had been expressed about the situation. However, he was afraid that one could reach some erroneous conclusions as to how the System ought to respond. As he recalled, the last time the System reacted in its policy decisions primarily because of foreign developments was when England went off the gold standard in 1931. At that time, with unemployment constantly increasing and with every element in the domestic economy calling for ease, the System responded by tightening in order to protect the gold supply. He was correct, he believed, in saying that every student of that action had concluded that it was a catastrophic blunder. Before beginning to respond to the international situation by means of monetary policy, he hoped the System would keep clearly in mind that it was errors in other fields, not in monetary policy, that had created the balance-of-payments difficulties. While abroad recently he had had discussions with bankers of a high degree of sophistication who must be aware daily of money flows, money rates, and exchange rates. Never once had one of them mentioned American monetary policy as a source of weakness of the dollar, while matters such as foreign aid and the budgetary program were mentioned many times. One could easily be led into great difficulty, Mr. Bryan said, if he thought that by the use of monetary policy the System could correct a situation that it had not created and that it could not fundamentally and basically correct.

Mr. Johns said he did not claim to have an answer to the manifestly hard dilemma with which the System was now confronted. On the one hand

there was the unsatisfactory state of the domestic economy, while on the other hand there was a disquieting balance-of-payments situation and outlook, with perhaps new evidence of deterioration in the confidence of the world in the dollar. To help his own thinking, Mr. Johns said, he had been trying to consider what it might be appropriate to do, in light of the domestic situation, if there were no balance-of-payments problem or if one were not aware of a problem, as may have been the case in the not too distant past. On that basis it seemed to him one might well come to the conclusion that the unsatisfactory state of the economy, as to which there seemed to be almost uniform agreement, reflected a situation in which the banks and the public at large still had unsatisfied liquidity desires. While the banks had done a good deal to repair their feelings of illiquidity, it was not possible to say as yet that they had altogether corrected that feeling. True, the banks had paid off a good deal of debt to the Federal Reserve, and they had accumulated more excess reserves than they had held for some time. Even so, however, they seemed unwilling to commit their reserves, or any significant part of them, to loans where the opportunity was afforded; or failing that, as would be rather typical at this stage of the cycle, to commit their reserves to significant amounts of investment. As to the liquidity desires of the public, which he thought were present and indicated, it was not quite clear how those desires were to be satisfied unless there was some significant expansion of bank credit. Unless those desires were satisfied, it seemed to him that the public would be likely to seek to

repair its feeling of illiquidity by further curtailing expenditures, and that meant more recession. On this premise--and he was still abstracting the other problem--it seemed to him that the monetary authorities should seek to supply reserves which would repair the banks' feeling of illiquidity and dispose them to bring about some expansion of bank credit, thereby to satisfy the liquidity desires of the public and to make the public more favorably disposed to consumption and investment. Having said that, he came back to the realities of the situation, for there was a very real balance-of-payments problem. As to what extent that problem circumscribed or even immobilized monetary policy, he did not have the answer. In a way it seemed to him that in the long run it would not be desirable, considering the balance-of-payments problem, to prolong the recession. However, he found himself favorably disposed to the suggestion that at this juncture the country should rely primarily on fiscal policy. Even though he had some reservations about the efficacy of an easy fiscal policy and a tight monetary policy, he would like to see fiscal policy used as quickly as possible. Pending the time, however, when fiscal policy could begin to take effect, it occurred to him that monetary policy ought to be moving cautiously and judiciously in the direction of repairing the feeling of illiquidity which he thought still pervaded the banking system and the public. If fiscal policy and monetary policy were both delayed until there had been a substantial deterioration in the economy, and particularly in unemployment and employment, the result might be more deterioration and

perhaps ill-advised fiscal maneuvers that would come back later to haunt everyone. Therefore, he could not bring himself to believe that the time was here for monetary policy to become restrictive; he would prefer to indicate that the System would not permit the reserve position of the banking system to deteriorate. In this connection, he had thought in terms of some modest increment of reserves, in the hope that it would be possible without too much delay to bring about an expansion of bank credit and, on the part of the public, a more favorable disposition toward consumption and investment. While he hesitated to suggest a figure, the $50 million increment suggested by Mr. Bryan for the next three-week period seemed reasonable.

Mr. Szymczak expressed the view, in the light of everything that had been discussed at this meeting, that monetary policy had been about right. However, he thought it would be desirable to explore further how fiscal policy, debt management, and monetary policy could best fit together in a period when there was a balance-of-payments problem. The possibility of operating in other areas of the Government securities market had been mentioned, and he would like to see that explored by the staff so the Committee might have a look at it. After all, the Committee should take a new look each time it met and had a new situation facing it.

After referring the recent developments that had been mentioned by Mr. Marget with regard to conversion of dollar balances into gold,

Mr. Szymczak said that regardless of whether monetary policy alone could do anything to relieve the problems related to the balance of payments, debt management, fiscal policy, and monetary policy, working together, should be able to do something to contribute to confidence in the dollar. His suggestion, therefore, would be exploration by the staff and the preparation of a paper for the Committee.

Mr. Balderston said that to him the policy followed by the Open Market Committee during the past year seemed in retrospect to have been a sound one. For at least ten months the System had been pressing reserves gradually on the commercial banks, and he had no regrets about what had been done to date. At the December meeting he had urged the Committee to continue to press reserves on the banks, with the thought that the banks would either lend or invest. At present it seemed to him one might well feel that the System had given the economy a full shot in the arm for the time being, that it had supplied the reserves that could be used constructively for a revival of the economy.

As to the gold outflow, Mr. Balderston commented that there seemed to have been a fundamental change in the situation. For many months the gold outflow was only a part of the total deficit, but now it appeared from the available figures that the gold outflow was greater than the deficit. If dollar holdings were declining at a time when the gold outflow was still large, that meant that the outflow currently was due in part to conversion of dollar balances into gold, not only by private individuals but by

foreign central banks. In view of that critical situation it seemed to him that the gold outflow needed to be given just as much emphasis in one's thinking as the domestic problem. He shared, of course, the view that the System must not attribute more to monetary policy than it merited. He remembered, for example, the British experience in 1955 when monetary policy was saddled with more of a load than it could carry in the absence of fiscal support. Therefore, he agreed that monetary policy alone could not turn the tide. It would take the support of the Treasury and especially of the Congress. However, he felt the time had come to stop pressing reserves aggressively upon the banks. In concrete terms, he would like to see the seasonal return flow of reserves mopped up completely, or almost completely, the yardstick being the Federal funds rate. He would like to see that rate at the discount rate, or very little below the discount rate, with the bill rate as high as it had been and if possible somewhat higher. The System had experienced good fortune in the large accumulation of bills by the Government securities dealers. Once they worked out of that situation, the bill rate would be under pressure, as he had thought it would be before this time.

In summary, Mr. Balderston said, he believed that the Committee should not only readjust its policy today but that it should watch developments during the weeks ahead with extreme care. He suggested the possibility of meeting again two weeks from today in order to keep on top of the problem.

Chairman Martin commented that he had been reviewing the minutes of the Open Market Committee, which he felt was a desirable procedure for all members to follow periodically. Sometimes statements attributed to him did not have quite the emphasis that he had intended, but this illustrated the difficulty of conveying all of the inflections of the comments that are made during a discussion involving a group of nineteen men. Thus, the operation of an account by a large group has some definite limitations. However, it also has some merit. Although sometimes too slowly, perhaps, at least for his own satisfaction, the discussions of the Committee do evolve a policy. On balance, he was inclined to think that there were advantages, as well as disadvantages, in the current procedure when working in so complex an area.

Continuing, the Chairman said it was his conviction at the moment that the policy of the Federal Reserve ought to be one of remaining steady in the boat. With a new Administration coming into office shortly, he thought that the Federal Reserve should not be moving drastically in either direction. In fact, if there was ever a time to be steady in the boat, it would seem to be right now. Having said that, he realized that the System must face up to the problems at hand. As had been mentioned a number of times, monetary policy cannot do everything. Mr. Bryan had pointed out well the 1931 experience, though he (Chairman Martin) wished to point out one significant difference between that situation and the present, namely, that in 1931 there was no question with respect to the credit of the United

States. As he had indicated at previous meetings, he felt that the principal shadow over the domestic economy was the problem of the balance of payments. True, that problem arose from a variety of sources, including foreign aid and military support programs and primarily, as Mr. Shepardson had mentioned, the shift from a seller's to a buyer's market which probably had finally come to pass.

Chairman Martin went on to say that, as indicated by the discussion this morning, there was occurring perhaps an evolutionary reappraisal of System policy. It is a good thing, he suggested, to have dissenting views before the Committee rather than to have all of the members thinking in the same pattern. In time, perhaps, all of those views would coalesce into a policy which would be a better policy than if everyone just followed along.

The Chairman said he did not think the time had come to increase the discount rate. Similarly, he thought it would be irresponsible to lower the discount rate at this juncture. The total problem, which was more serious than generally appreciated, involved more than an outflow of gold. Rather, it reflected uncertainties in the whole world situation. For example, there was the situation in the Congo and the Cuban problem, along with the fact that the pound sterling was not quite as strong as it might be. Accordingly, in terms of the gold supply of the world the tendency of people in many places was to think that the situation might be heading toward a world economic crisis of some sort.

Personally, he did not believe that that was going to happen. Nevertheless, it was incumbent upon the System to recognize that it was possible for people to prefer gold to any currency. Some leakage of gold was occurring, reflecting not only uncertainties about the dollar but about world institutions generally. The dollar, which had stood out as a symbol for a long period of time, had now lost some of its polish. In his opinion, this was the foremost problem that the new Administration would have to face, but he hoped that the System would not get too excited and that it would feel its way along in terms of policy.

Chairman Martin then commented on difficulties of phraseology, pointing out that terms such as "aggressive ease," "less aggressive ease," and "less easy" all may mean different things to different people. Therefore, he could understand the problem of the Account Management. However, he felt the general consensus today probably was in the neighborhood of maintaining the status quo and that the majority did not want to move too much in either direction.

The Chairman said that personally he would not want to appear to be embarking on a policy of sloppy ease at this moment. As Mr. Johns had pointed out, the banks were not quite as liquid as they would like. On the other hand they had made great strides in that direction. The Chairman was not sure that forcing the banks too much toward seeking loans aggressively would be a service to the people to whom they would lend the money at the present time. Profit margins and other business

factors would be under close review. As noted by Mr. King, probably the period when productivity and wages had little relationship had come to an end.

All of these things should be taken into consideration, Chairman Martin said. With only a short time remaining before the new Administration came into office, and in view of the fact that the country was in the midst of a gold outflow, in his opinion the Federal Reserve should remain steady. It was difficult, he suggested, to assess how mild the outflow of gold actually would be. In his own mind he saw a certain similarity between this period and the period of pressure on the bond market in 1951 in the sense that at that time people were saying each day that there was no real pressure because only a limited volume of transactions had taken place. As at that time, however, there were forces accumulating which, unless properly handled, might lead to real trouble. As to the gold problem at the moment, no one could really correct it except the incoming Administration.

The Chairman went on to say that he was by no means pessimistic and that he felt the business picture was perhaps better than generally realized. As he had said before, in his view the biggest shadow over it was the balance-of-payments problem, which exerted an effect in many ways that were not generally appreciated, including the willingness of banks to extend credit. This was something that it had not been necessary to deal with in this country for many years, and therefore the problem had drifted out of the area of serious discussion for a long time.

After referring to the volume of suggestions currently being made for various courses of action that might be taken in dealing with economic problems, the Chairman said it was still a fact that the economy was doing surprisingly well and that there was surprisingly little real suffering. This was not to say that there was no suffering among the unemployed, but the situation was not one of panic or disaster and the strong points in the economy should not be ignored.

At this point Chairman Martin referred to the suggestion of Mr. Balderston that the Open Market Committee meet again in two weeks. With a new Administration shortly to take office, and in view of the fact that the country was experiencing a continuing gold outflow and a good many ideas about economic problems were being passed around, he felt that it would be the part of wisdom for the Open Market Committee to plan to meet in two weeks and then again after another two-week period. This would afford an opportunity for the Committee to be brought up to date on problems of transition between Administrations, to keep abreast of developments, and to have discussions such as had taken place this morning.

Chairman Martin then commented that no specific change in the directive had been proposed at this meeting. He again stated that he thought the consensus was to hold close to the status quo.

The Chairman inquired of Mr. Robertson whether he would like to be recorded as dissenting, and the latter replied by expressing agreement that the consensus stated by the Chairman reflected the majority view.

No further comments being heard, Chairman Martin stated that, as usual, each person's views would be recorded fully in the minutes.

Thereupon, upon motion duly made and seconded, it was 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 encouraging monetary expansion for the purpose of fostering sustainable growth in economic activity and employment, while taking into consideration current international developments, 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.

Pursuant to Chairman Martin's suggestion, it was agreed that the next meeting of the Federal Open Market Committee would be held in Washington on Tuesday, January 24, 1961, and that the succeeding meeting would be tentatively scheduled for Tuesday, February 7, 1961.

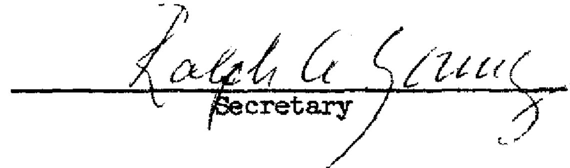
Mr. Johns commented that plans were in process for a meeting of the Conference of Presidents of Federal Reserve Banks on Monday, March 6, 1961, with thought that a meeting of the Board and the Presidents would be held the following day. After a brief discussion, it was understood that this schedule would be continued to be used as a basis for planning.

At this point all of those present withdrew from the meeting except the members and alternate members of the Committee, the Reserve Bank Presidents who are not currently members of the Committee, and Messrs. Young and Rouse.

During the course of a discussion, Chairman Martin suggested that the Ad Hoc Subcommittee that had been authorized at the meeting on May 17, 1951, and which submitted its report under date of November 12, 1952, be reactivated for the purpose of studying certain aspects of open market operations, with the membership of the Committee increased to include the Vice Chairman of the Federal Open Market Committee and the Vice Chairman of the Board of Governors. With this adjustment the membership of the reactivated Committee would include, in addition to Chairman Martin, Messrs. Balderston, Bryan, Hayes, and Mills. The Chairman also suggested that Messrs. Young and Rouse be designated to serve as technical advisers to the Committee.

This suggestion was approved unanimously, with the understanding that Chairman Martin would initiate studies by the Committee at such time as he decided was appropriate.

Thereupon the meeting adjourned.



Secretary