A meeting of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System in Washington on Tuesday, May 29, 1962, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman 1/
Mr. Hayes, Vice Chairman
Mr. Balderston
Mr. Bryan
Mr. Deming
Mr. Ellis
Mr. Fulton
Mr. King
Mr. Mills
Mr. Mitchell
Mr. Robertson
Mr. Shepardson

Messrs. Bopp, Scanlon, Clay, and Irons, Alternate Members of the Federal Open Market Committee

Messrs. Wayne and Swan, Presidents of the Federal Reserve Banks of Richmond and San Francisco, respectively

Mr. Sherman, Assistant Secretary
Mr. Kenyon, Assistant Secretary
Mr. Hackley, General Counsel
Mr. Noyes, Economist
Messrs. Brandt, Brill, Furth, Garvy, Holland, Koch, and Willis, Associate Economists
Mr. Stone, Manager, System Open Market Account
Mr. Coombs, Special Manager, System Open Market Account

Mr. Molony, Assistant to the Board of Governors
Mr. Cardon, Legislative Counsel, Board of Governors
Mr. Williams, Adviser, Division of Research and Statistics, Board of Governors
Mr. Knipe, Consultant to the Chairman, Board of Governors
Mr. Yager, Chief, Government Finance Section, Division of Research and Statistics, Board of Governors

1/ Entered meeting at point indicated in minutes.

Mr. Francis, First Vice President, Federal Reserve Bank of St. Louis
Mr. Hickman, Senior Vice President, Federal Reserve Bank of Cleveland
Messrs. Eastburn, Ratchford, Baughman, Jones, Tow, Coldwell, and Einzig, Vice Presidents of the Federal Reserve Banks of Philadelphia, Richmond, Chicago, St. Louis, Kansas City, Dallas, and San Francisco, respectively
Mr. Sternlight, Manager, Securities Department, Federal Reserve Bank of New York
Mr. Hellweg, Economist, Federal Reserve Bank of Minneapolis

Upon motion duly made and seconded, the minutes of the meeting of the Federal Open Market Committee held on April 17, 1962, were approved.

Before this meeting there had been distributed to the members of the Committee a report on open market operations in United States Government securities covering the period May 8 through May 23, 1962, and a supplementary report covering the period May 24 through May 28, 1962. Copies of both reports have been placed in the files of the Committee.

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

Among the more noteworthy developments as viewed from the Trading Desk since the last meeting of the Committee is the fact that while the banking system has had continuously available a volume of free reserves that is within the range of other recent periods, there has occurred, behind that volume of free reserves, a considerably more comfortable money market situation and a perceptible slowing of the rate of growth of total reserves. The evident implication is that the economy has been making less vigorous use of available free reserves than in April, for example, and, in the past week or two, less vigorous use than one might expect on seasonal grounds. A part of the explanation of this situation, as we see it from the vantage point of the Desk, lies in the sharp reductions in dealer positions and use of credit since late April and early May, but whether and to what extent the explanation for the less vigorous use of available reserves in the recent period goes beyond the decline in dealer financing requirements is difficult to determine. In any event, with Federal funds largely in a 2 - 2-3/4 per cent range, the reserves have clearly been available in ample volume. Mr. Holland, in his broader review of the credit situation, may have somewhat more perspective on these matters.

Given this new situation, rates on Treasury bills moved lower during the early part of the period, but turned upward when the Treasury announced that it would add $100 million to the bill supply in the auction held last week (and when it subsequently announced that another $100 million would be added to the bills sold in yesterday's auction). Demand for bills has been good throughout the period, and the general tendency has been toward lower rates. Yesterday, partly in response to the easy money market that developed, the rate moved lower again. The three-month bills were sold at an average of 2.66 per cent, while the six-month issue was sold at an average of 2.74 per cent. These rates are down 4 or 5 basis points from the preceding auction but are close to the rates set in the auction two weeks ago. If the economy does not use the reserves available to it any more vigorously than in the recent period, then assuming free reserves in about the recent range, bill rates could well drop somewhat further even if the Treasury continues to add $100 million to the supply of bills for the next two or three weeks. If, on the other hand, the economy should use up reserves at the rate it did in April, short-term rates could well tend to move upward.

Prices of Treasury bonds in the period since the last meeting were up, then down during much of the period, and finally up again in the past several days. The rise at the beginning of the period was more or less a continuation of the upward movement that had started about three months ago, when the market seemed to decide that neither economic trends nor developments in credit policy would put upward pressure on longer-term rates for the time being -- and that the balance of forces on rates might even be downward. The rise in prices gained further impetus from the steady erosion of stock market prices. Then, from about May 14 through 21, bond prices fell off and in some cases lost perhaps a third of the gains recorded over the previous two and a half months.

Better news about the economy, the approaching payment date for the May refunding, and sporadic advances in the stock market all helped to produce a much more cautious attitude among dealers -- who still held large amounts of the refunding issues and sizable inventories of other issues as well. While there was no heavy selling by investors, the limited offerings that did appear were not readily absorbed--and in fact dealers sought instead to lighten their inventories of intermediate and longer issues at every opportunity. A second turnabout in the price trend came around May 21-22 as fresh buying was stimulated by the more attractice yield levels than attained, and by the new rush of price declines in the stock market, while dealers' inventories had by this time worked down to a considerably lower level. Throughout the period it was evident that the stock market was a major factor influencing the prices of Treasury securities--both as a psychological factor and as a direct influence as some funds reportedly moved out of equities and into fixed-income securities. The stock market's influence was particularly noteworthy yesterday, when the bond market started out with small price declines, and then turned around as selling pressures mounted in the equity market.

Finally, I might comment on the question raised by Mr. Swan at the last meeting of the Committee, with regard to the recent use of repurchase agreements. We discussed this matter informally after the last meeting and it might be useful to summarize here the substance of that discussion. You may recall that Mr. Swan asked two questions--first, whether the recent use of repurchase agreements went somewhat beyond the rationale originally envisaged when the repurchase instrument was adopted; and second, whether the recent use of repurchase agreements had a tendency to cause reserve levels to turn out somewhat lower than anticipated because of dealers' action at times in terminating these agreements before maturity. On the first point I think the answer is "yes"; it seems to us that a somewhat more extensive use of repurchase agreements has been part of the process of adapting System open market operations so as to be able to inject reserves while minimizing direct downward pressure on bill rates. As to the second question, it does not seem to us that the employment of repurchase agreements has tended to produce significant shortfalls from anticipated reserve levels. We know when we arrange these agreements that they may be withdrawn by dealers prior to maturity, and some rough allowance can be made for this. Partly for this reason, shortfalls from anticipated reserve levels owing to dealer withdrawals of repurchase agreements have been very small relative to shortfalls resulting from the erratic behavior of market factors.

Thereupon, upon motion duly made and seconded, the open market transactions in Government securities during the period May 8 through May 28, 1962, were approved, ratified, and confirmed.

Mr. Noyes presented the following statement with respect to economic developments:

At one time or another in recent months almost every analyst of economic developments has found occasion to express some doubts as to the sustainability of the level of stock prices. In many of the forecasts for 1962 made at the close of last year, a major break in equity prices was mentioned as one of the disturbing possibilities. At the first of the year, and several times thereafter, it seemed that such a major adjustment might be under way, but until mid-March each was reversed after a short drop. Since March 15, however, prices have been declining, with only minor interruptions and growing momentum, until at the close yesterday the Standard and Poor's average at 55.50 was off 24 per cent from the December high. The fact that the adjustment was so widely heralded does not seem to have substantially reduced either the dismay or the pain of its reality.

There can be little doubt that a decline of these proportions must be reckoned as a major factor in any appraisal of economic developments. While the effects should not be exaggerated, they have already spread well beyond the narrow confines of the market itself. Whether it should be or not, a drop this large will be interpreted by many as a harbinger of recession. It will almost certainly result in some curtailment in investment expenditures and perhaps dampen consumer spending as well, especially for luxury-type goods and services.

The stock price decline has proceeded in the face of quite a bit of relatively favorable news with respect to the performance of the economy. Production in April was up a little more, if anything, than we estimated at the time of the last meeting. Indications are for some slight further gain in May, despite the curtailed rate of steel production.

Retail sales were up about as anticipated last month, and both department store and auto sales continued strong through the first three weeks of May. Neither our own buying intentions survey taken in mid-April or the current information received from other surveys provides evidence of slackened consumer confidence or a cutback in consumer spending plans. In fact, the surveys, taken together, would suggest some pick-up in demand for household durable goods, an area which has lagged thus far in the recovery and expansion.

Housing starts were up further last month, and house purchase plans reported in the survey also showed some improvement. Consumer credit growth in April is now estimated at almost half a billion dollars--up somewhat more than the early figures on retail trade would have indicated, and considerably above the previous high for this recovery period.

While developments have not taken on any of the characteristics of a boom, one would have had to have rather high hopes to find the performances of the economy so far in the current quarter disappointing with respect to current sales, output, and employment.

But, apart from the stock market, there has been evidence of concern and even pessimism regarding the economic outlook. Information reported by the National Association of Purchasing Agents with respect to their plans and policies has taken a very pessimistic turn. Observers who rely heavily on the National Bureau of Economic Research leading indicators have found, especially in certain combinations of these statistics, configurations which lead them to suspect that a downturn may not lie too far ahead. The behavior of manufacturers' new orders for durable goods--which declined for two months and showed no improvement in April--has been disappointing to some.

While they are not as specific and articulate as one might wish as to their reasons, businessmen in a variety of lines report dissatisfaction and concern--and this feeling on their part is an economic fact which must be taken into account, along with the data.

Even before the dramatic further decline in the market yesterday, it seemed clear that quite a fundamental reappraisal of the economy's performance and prospects, especially as to profits, was under way. It is hard to think of any constructive change in policy that the monetary authority might take while this reappraisal is in process. The continuation of a policy aimed at the objectives expressed in the current directive would seem most appropriate.

Mr. Furth presented the following statement on the U. S. balance of payments and related matters:

In April and May, balance of payments developments were midly encouraging. For the first quarter, official balance of payments data showed a monthly deficit of $150 million. But the figure based on net transfers to foreigners of gold, convertible foreign currencies, and dollars would be around $200 million. The Board's staff believes that the latter figure is better comparable with current data.

The deficit for April was $200 million, about the same as the first quarter average but much less than the figure for March alone. Tentative and partial data for the first three weeks of May indicate further improvement this month.

Net gold sales to foreigners amounted to a monthly average of $100 million in the first quarter and to $120 million in April, but to only $60 million in May. Our net sales for this month were reduced by some gold purchases, mainly from Canada.

Economic activity abroad remains satisfactory in the developed countries but mixed in underdeveloped areas. Output in the United Kingdom seems to be expanding; the country's balance of payments appears to be in equilibrium, with a rise in exports apparently to a large extent offsetting the decline in the inflow of capital funds. Concern has been expressed, however, about pressures for wage increases in excess of amounts deemed compatible with the maintenance of price stability.

Similar concern is prevalent in Continental Europe although the continuing rise in the reserves of the main European countries makes anxiety about the competitiveness of European industry appear premature, to say the least. The Gilpatric agreement with Germany on military expenditures and agreements with Italy and France on debt prepayments will temporarily reduce both the European surplus and the U. S. deficit, but the prepayments will not correct the underlying situation.

Continuing financial, economic, and political troubles in many Latin American countries will probably put a double burden on our balance of payments and on our domestic economy: they will hamper our exports to those countries, and at the same time increase pressures for additional government aid.

Gold and foreign exchange markets were quiet until a few days ago. Since last week, however, the markets have been nervous, with unfavorable effects on the dollar. Some of the reasons were technical: the continuing concern about the future of the Canadian dollar has apparently led to the withdrawal of European funds from Canada; and since the U. S. dollar is invariably used as "vehicle currency" in these transactions, the movement has strengthened the U. S. dollar vis-a-vis the Canadian dollar but weakened it vis-a-vis the European currencies. Similarly, the apparent cessation of capital flows from the Continent to Britain has strengthened the dollar against sterling but contributed to dollar weakness on the Continent.

But there have also been rumors about withdrawals of European funds from the New York stock market. If such withdrawals became substantial, they would weaken not only the dollar rate but also our balance of payments.

Whatever the reason, the dollar is again close to the floor against all major Continental European currencies except the German mark. It has improved against sterling, although still remaining below par. It has risen substantially above par against the Canadian dollar, but this is scant comfort.

Even the London gold market, which had been a bright spot in the international financial picture in recent months, has been disappointing. The price has again risen above $35.08, and the Bank of England had to sell some gold to the market.

In absolute terms, all these movements have not been very impressive. When seen in context with developments on the stock exchange, however, they may be taken as another symptom of disturbed investor confidence and the resulting general market uneasiness.

Mr. Holland presented the following statement with respect to credit developments:

Banking and credit changes during the past three weeks have been pushed into the background by the eye-catching developments in the central financial markets. Mr. Noyes has already commented on the dramatic decline in the stock market.

The municipal market has also been under some pressure, with yields backing up somewhat as dealers worked to move sizable new offerings in the face of a record total of inventories on the Blue List.

Meanwhile, the Government securities market has been the focus of conflicting influences. For a time during May, it appeared the market yield curve was destined to lose some of the flatness it had acquired during 1962, as downward market pressures on the bill rate were followed by upward pressures on yields extending from the intermediate through the long end of the Government list. Such pressures were countered in varying degrees by System and Treasury actions to bolster the bill rate and by the strength imparted to the debt markets by sinking stock prices. As a consequence, the month of May drew towards its close with a yield curve in the Government market not far different from that at the beginning of the month, despite some tendency for other short rates to move lower and long-term municipal yields to move higher. Now, however, a combination of resurgent investor demands and the temporary reserve surpluses of the current week are applying new downward pressures particularly on the bill market, and it remains to be seen how much bill yields will be displaced by this convergence of factors.

During this span, the banking system has continued to add to its loans, although in a somewhat altered pattern. In the first half of May, loan growth in the smaller urban and rural areas appeared to slow, while loan increases at city banks were stronger. In part, the increases in loans at city banks represented temporary or one-time influences, such as the short-run financing of enlarged dealer positions around the Treasury financing and the taking into portfolio of almost all the $300 million participation certificates sold by the Export-Import Bank. Underlying these changes, however, were some further increases in real estate, consumer, and business loans. Among the cyclically strategic industries, only construction has accounted for an important part of the business loan increases of recent weeks. Loans to construction firms by leading banks have been moving up briskly since March, paralleling the pickup in building activity.

Bank holdings of securities appeared little changed on balance during the past four weeks. This resulted in less total bank credit expansion than had been reported for some previous months or for the comparable period of last year. Bank holdings of municipal securities declined a little for seasonal reasons, due chiefly to the maturity of some New York City tax notes. Even after allowing for that factor, however, the more gradually mounting figures reported for recent weeks suggest some waning in bank appetites for more municipals, at least at the yield levels prevailing during April and much of May.

Turning to the deposit side of bank balance sheets, reports indicate a slower rate of increase in time deposits, a pause in expansion of demand deposits, and a large shift of demand balances from private to Government hands. As a result, the average money supply in the first half of May is estimated to have slipped about $100 million following its billion dollar April increase, and a larger reduction is possible in the second half of this month. At its mid-May mark, the money supply stood 2.8 per cent above its year-ago level. Available data suggest a continuing increase in the rate of money use. Turnover of demand accounts in reporting centers outside New York reached an annual rate of 31.8 in April. Thus far during 1962, deposit turnover so measured has averaged 8 per cent above a year ago.

Reflecting these deposit movements, the total of reserves required against private deposits declined substantially more than seasonally during the first three reserve weeks in May. The level reached in the week of May 23 was equivalent to a 3 per cent annual rate of growth in such reserves from last November. Furthermore, the full amount of that increase in aggregate reserves over the past six months was more than taken up by the growth in reserves required against time deposits; reserves required against private demand deposits were actually below their November level on a seasonally adjusted basis.

The May contraction in the private reserve base substantially offset the April increase, despite the fact that free reserves were maintained during the month at an average level substantially unchanged from April. In fact, free reserves in this week and last are relatively high compared with typical 1962 levels. Such a pattern calls attention to the fluctuating nature of private deposit totals, and warns against the imputation of significance to the movements in individual weeks except as they can be seen as parts of a developing pattern. Distortations or concentrations of deposit movements can be created by the erratic timing of many bank loan and investment decisions, a particular case in point being securities loans. Another major contributor to private deposit fluctuations--and a key factor recently--is the change in Federal Government accounts. Treasury balances dropped to unusually low levels through April, and then rose probably to a record average level in May. They are likely to persist at a relatively high level during much of June. Such movements have thus served, first to expand, and more recently to contract, private money holdings for appreciable spans of time. Shifts of deposits into Treasury accounts during May also led to some concentrations of reserves in the major money centers. This movement may provide a partial explanation of the development of easier money markets along with more or less stable free reserve figures, and perhaps also may have influenced the appearance of stronger city bank loan expansion along with a slackened pace of expansion in outlying areas.

The conduct of System operations in the weeks immediately ahead will continue to be complicated by such Treasury influences, above and beyond the more predictable reserve impacts of a heavy currency drain over the next statement week and the usual early-month trough and midmonth bulge in float. An appropriate policy to guide such operations must take into account many considerations, some of which lie outside the scope of this review. With slackened bank credit expansion, a contracting money supply, and unsettled conditions in key financial markets, however, any move toward more restrictive general monetary conditions than prevailed during the earlier weeks in May would appear out of step.

Chairman Martin, who had been attending a meeting at the White House, entered the room at this point.

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

> I would like to preface my remarks by stating that I wish our meeting were not occurring only one day after yesterday's momentous happenings, as the visibility this morning is certainly low. However, I have in mind the fact that we must set policy for three weeks ahead, and hopefully the atmosphere may be very much less hazy a week or two weeks hence. It therefore seems appropriate to consider what might be done if and when the dust clears.
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> Most business statistics in April were rather satisfactory and indicative of a continuing gradual rise in business activity. Retail sales and housing starts were particularly encouraging. With personal income continuing upward, the foundation is being laid for further gains in consumer spending. As for business spending, the outlook is clouded by the possibility of repercussions of the steel price episode on business attitudes. A clear line on capital spending plans subsequent to the steel episode must wait on the Commerce-SEC survey, which will become available in June. Inventory accumulation in the current quarter will be far below that of the first quarter, primarily because of the situation of the steel industry.
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> One major uncertainty is the effect on spending of the sharp drop in stock prices. While experience in the past few months does not show any clear effect of lower stock prices on consumer or business spending, there is no doubt that the market decline reflects an undercurrent of distrust, both here and abroad, that could act as a check on the current expansion. A more optimistic interpretation might construe much of the stock price drop as an adjustment to a noninflationary environment; but even if the decline stemmed from this worthwhile reason it could nonetheless generate some highly undesirable effects of its own. Commodity prices continue to exhibit marked stability, especially at the wholesale level.
>
> Regardless of the expected improvement in business, it seems increasingly doubtful that unemployment can be reduced to the so-called "tolerable level" of 4 per cent even a year from now.
>
> Credit demands have been quite moderate, and there has been a good balance between the supply of, and the demand for, credit and capital. The loan officers and economists of major

New York City banks are still concerned over the failure of loan demand to develop as expected earlier, and they do not look for much change in the immediate future. Clearly, most banks throughout the country are in a comfortable position to meet all legitimate credit requests. It might even be contended that they have been enjoying an excessive degree of liquidity which has tended to put undue downward pressure on short-, medium-, and long-term yields. Since the heavy seasonal Treasury deficit in prospect for the second half of the calendar year will necessarily be financed in good measure by the banks, the latter will experience a significant increase in liquidity as a consequence of this development. As for nonbank liquidity, while it is always very difficult to judge its adequacy on the basis of the various statistical measures available, I have a general impression that it is relatively comfortable at the present time.

The balance of payments outlook remains unsatisfactory. Although the over-all deficit in April improved somewhat over the high March figure, it remained above the first quarter average, after adjustment has been made for the French advance debt repayment last month. Merchandise exports seem to have been weakening significantly, and there has been an increase in long-term borrowing in this market by foreigners. While we should not give too much weight to any single month, the fact remains that the balance of payments for the year to date shows a disappointing lack of improvement over a year ago. During the past week the dollar has been under some pressure in the exchange markets, partly because of nervousness as to possible protective measures that might be adopted by the United States. With foreign dollar holdings continuing to increase, there is reason to look for declines in the gold stock over the coming weeks.

Some months ago the hope was expressed in our meetings that a "natural" increase in interest rates accompanying further cyclical business expansion might help to dampen the outward flow of capital from this country. However, recent business and credit developments do not point to the likelihood of such a tendency in the near future. Monetary policy continues to face a dilemma with respect to the emphasis that should be placed on domestic and international considerations, and the dilemma is perhaps becoming more acute as the balance of payments deficit continues in the face of a rather slow rate of domestic business expansion.

I am aware that most of the Committee members have been exceedingly reluctant to consider any deliberate tightening of credit conditions in view of the domestic situation, and the severity of the stock market break would naturally strengthen this reluctance.

I have considerable sympathy with this view; nevertheless, I believe that if and when the stock market shows signs of bottoming out and stabilizing we might probe in the direction of somewhat less ease, with the hope of encouraging the 90-day bill rate to hold closer to 3 per cent than to 2-3/4 per cent, a Federal funds rate consistently close to the discount rate, and some pressure on the banks' bill portfolios. The liquidity of the economy seems ample to give some leeway for such probing. Although only experience can disclose what this might mean in terms of free reserves, it seems to me likely that these objectives could probably be achieved with free reserves in the $300 to $400 million range. I would stress that what I have in mind is cautious experimentation, with close attention being paid to any possible adverse effects of such probing on the continued expansion of bank credit and bank deposit. Incidentally, I have in mind that even-keel considerations may be with us again shortly after the next meeting. With respect to bill rates, it seems to me that we have been leaning rather too heavily on the Treasury's debt management policies (i.e., adding to the weekly bill issues) to keep these rates at acceptable levels, especially in view of the fact that the Treasury must do a great deal of cash financing in the next six months. I would repeat that any probing towards less ease should be undertaken only if the stock market regains some measure of composure.

With respect to the directive, I had thought that one of the reasons behind our change in procedure a few months ago was to provide for greater flexibility, i.e., to avoid a tendency to continue in effect for months on end a directive which was very general in character. The present directive has remained unchanged since March. I suggest that we amend it today to indicate the current economic situation (including particularly the stock market break), the ample liquidity situation, and the need for some slight shift in emphasis in view of our serious balance of payments problem.

More broadly, I am wondering more and more whether the current "mix" of monetary policy and fiscal policy is the best that could be devised to meet the combination of internal and external problems which we face. I am interested to observe that the possibility of a tax reduction as a means of stimulating the economy is apparently receiving study. Successful action along these lines would of course give monetary policy greater leeway to exercise a dampening influence on the outward capital flow.

Mr. Bryan said he had left for this meeting prepared to say that the business situation seemed to be developing in such manner, both nationally and in the Sixth District, as to suggest some lowering of the Committee's free reserve target and the establishment of a lower growth rate than he had heretofore been advocating in regard to total reserves. However, after the events of yesterday, he could not advocate any monetary policy except one of continued ease. Mr. Noyes had spoken well, he thought, of the influence of the equity market break on consumption and on investment. The stock market developments could affect millions of people who did not hold a single equity security and simply read about the matter in the press. As to investment, it was the policy of many corporations to try to maintain a certain proportion between their debt and equity instruments. Where such corporations had been contemplating equity financing, they would now be reluctant in many cases to go forward. In addition, he was afraid that the stock market break was going to have a reaction that would not be helpful to the banking situation. He would imagine that many banks had gotten under way studies of their loans, and that their standards of lending were going to be raised. That would be particularly true, he believed, in the case of banks that had over the past three or four years piled up a substantial volume of demand loans secured by high-grade equity and debt instruments. While such loans might actually be demand loans in New York, and to a lesser extent in Chicago, in the outlying banks of the country they were long-term capital loans on which neither the borrower nor the lender expected repayment to be made, the funds being used by the borrower for long-term capital commitments.

In such circumstances, Mr. Bryan repeated, he was not prepared to advocate any change in monetary policy. It seemed to him that the Committee must continue to supply reserves in seasonal amounts, plus some modest growth factor, say 3 per cent.

Mr. Bopp reported that the Third District was experiencing the same kind of gradual business upswing as the nation, although as usual there was a tendency for the District to lag behind the United States. Such up to the minute data as were available indicated no general acceleration in the upswing.

In banking, on the other hand, the picture was quite different. Business loans in the District, unlike the nation as a whole, had been experiencing a sharp pick-up. The increase was widely based among almost all industrial categories. Reserve positions were comfortable, borrowing from the Reserve Bank was negligible, and reserve city banks were still net sellers of Federal funds, although in smaller amount.

If it were not for the balance of payments problem, Mr. Bopp said, he would like to see an easier monetary policy, especially after the developments in the stock market yesterday. Although policy to date had been successful in promoting a high degree of liquidity in the banking system and the economy and had helped to keep long-term rates from rising, it was probably true that still greater ease could further stimulate the rather sluggish demand which, at least in part, was behind the current relatively moderate rate of economic expansion. The question had been, and remained of course, whether further ease could accomplish enough domestically to warrant possible further aggravation of the balance of payments situation. He was inclined to doubt it. In view of the possibility that the balance of payments might worsen during the course of the year, substantial further ease could well be too great a risk.

Accordingly, Mr. Bopp said, he would be inclined to continue monetary policy essentially unchanged, especially in view of the stimulating effect likely to ensue from a rising budget deficit. At the same time, he would also like to see the Desk continue to probe in the direction of lower long-term rates by purchasing intermediate- and long-term issues when appropriate and selling short terms if necessary to accomplish this. He would continue about the same degree of ease in reserves, maintain the present directive, and leave the discount rate unchanged.

Mr. Fulton reported that, except for the retail sales sector, economic activity in the Fourth District had worsened considerably in recent weeks, trends in unemployment, electric power output, and steel production having been unfavorable. Auto sales had been maintained in the three major cities of the District at a vigorous rate, and it began to look like a 7 million car year, including about 350,000 imports. Reports for May on department store sales showed them expanding to a new high. For the year to date, such sales were up 4 per cent from a year ago. However, the unemployment picture had shifted into the unfavorable category in May. Contraseasonal layoffs had occurred, concentrated largely in the steel areas. Unemployment was up three per cent in the District from late April to mid-May. As to the steel industry, Mr. Fulton described the current picture as dismal, with no pick-up in orders and ingot production continuing to drop. Steel users, including the automobile industry, still had substantial inventories. Construction was in good volume in the major cities of the District, which provided a bright spot.

Turning to the banking picture, Mr. Fulton said that commercial and industrial loans had dipped. In the three weeks ended May 23, they declined by the largest amount of any week since January 3 of this year. Demand deposits adjusted were down sharply, while savings deposits continued to increase.

As to monetary policy, Mr. Fulton expressed the view that the System had done about all it could in terms of the domestic economy. The System had consistently supplied reserves in quantity; it had met all of the seasonal factors and had provided an additional factor for growth. Credit had been readily available, but was not used by businesses. It appeared to him that international considerations predominated at present and that free reserves might well be reduced. Thus, he would go along with a range of $300-$400 million in lieu of figures over $400 million. Also, while recognizing that the margin requirement instrument was not within the province of the Open Market Committee, he felt that a reduction in margin requirements might be considered. Confidence had been shaken, to put it mildly. Likewise, the international situation involved a confidence factor. Some confidence might be restored, in his opinion, by a reduction of margin requirements and by a firming of interest rates through making fewer reserves available.

Mr. Fulton said that he would not recommend changing the discount rate at this time. He would have no objection to renewing the present policy directive, although it might be changed somewhat to reflect existing economic circumstances more precisely.

Mr. King said he thought it had been fairly generally agreed that a stock market correction would necessarily come about at some point. The concern he had today was that the ramifications of the stock market decline not spread further than necessary. He did not believe that the System could control or stop the stock market slide, but it should do whatever was possible to allow natural forces to bring about a cessation of the decline.

Mr. King went on to say that he thought the Open Market Committee had contributed to the defense of the dollar by doing what it could to maintain the bill rate. The Treasury, of course, had done a great deal through measures such as adding to the supply of bills. Three or four months ago, however, he (Mr. King) had spoken to this point and said that he thought the Federal Reserve should cease its efforts to maintain the bill rate within a particular range.

The more the System tried to hold short-term rates in this manner, the more he felt that the stock market decline was likely to continue. With that thought in mind, he would suggest that there be deleted from the policy directive the reference to minimizing sustained downward pressures on short-term rates. A time might come when the bill rate level could no longer be maintained, and in his opinion it was better to cease the effort before that time came, although he would not advocate that the System and the Treasury pursue different objectives. At one time, he recalled, he had been a leading proponent of maintaining the bill rate, and he thought this had served a desirable purpose. He was surprised that it had been possible to keep the bill rate in its present range for so long. However, he felt that the time was coming when this would no longer be possible.

Mr. Mitchell said it was his general feeling that present System policy was about the best that could be devised at this particular time. He did not see that there was any change that would be particularly helpful. If there was to be a move in either direction, he would think that a slight easing would be preferable. On the other hand, the reverberations of stock market developments seemed likely to make this country's balance of payments position somewhat more serious than it had been. The psychological reverberations about which the Committee had been worrying might come into play. On the domestic side, there would be, unquestionably, some reaction on consumer spending, particularly for hard goods, if the stock market continued weak and prices declined further. All in all, this was a bad day to make policy decisions. Under those circumstances, it would seem best to wait and make no change for the moment.

Mr. Shepardson spoke of having attended yesterday a meeting of representatives of institutional lenders to agriculture, at which there were reports of a continuing rise in farm land prices. The drop in land prices in the corn belt area had been completely recovered, and prices in other areas were continuing to move upward. Most institutional lenders represented at the meeting reported a rise in farm mortgage lending. Several insurance companies, finding inadequate outlets for their funds elsewhere, were providing their farm departments with increased allocations of funds. Concessions were being made on rates. Some country bank representatives mentioned that while their construction loans, particularly residential, had not shown much increase as yet, they had all made heavy advance commitments and had been delayed in putting out the money, only because of weather conditions.

Mr. Shepardson also reported that at yesterday's meeting there was discussion of the foreign trade situation and the potential effect of the European Common Market agreements on agricultural exports from the United States. Question was raised as to whether farm land prices were not being pushed out of reason, considering the prospects for crop prices.

All of this, Mr. Shepardson said, strengthened the feeling he had had for some time that perhaps the System had accomplished all it could do through monetary policy and that it should be drawing back a little, at least on the rate of growth of reserves. He had spoken at previous Committee meetings in favor of reducing the annual rate of growth of total reserves to 3 per cent, or even lower, and he had felt surer of that position after attending the meeting yesterday. However, when he learned of the gyrations in the stock market, he felt much like Mr. Hayes, that no perceptible change in policy should be made at this time. Nevertheless, as soon as the situation cleared somewhat, he believed that a careful look should be taken at the amount of funds available in the market to appraise whether the System was going to aid the domestic situation by continuing to supply reserves so liberally since corrections in the domestic situation might well have to come from other factors. The System should study whether the uncertainties generated by the stock market situation and their impact on the balance of payments situation did not call more than ever for a position of less ease as soon as the visibility improved. In summary, his position was similar to that expressed by Mr. Hayes.

Mr. Robertson expressed the view that the Committee should refrain at this time from being panicked into any action that might develop to be unfortunate. This was the time when an organization like the Federal Reserve System ought to stand out as an example for the nation. It should hold as steady as possible.

Mr. Mills commented that if a loss of public faith in the stability of financial conditions was being experienced, the thing needed to restore confidence was the injection of some degree of discipline into the financial markets under the leadership of the Federal Reserve System. Unhappily, in the light of the circumstances in the stock market, he believed, like others who had spoken, that any overt change in policy at the present time would be misunderstood and would be more disturbing than tranquilizing. However, every opportunity should be taken by the System to inject some discipline into what he considered a very soft and weak monetary and credit policy situation. To elaborate on his thinking, Mr. Mills presented the following statement:

> Over many months past, repeated opportunities have opened up for changing the direction of Federal Reserve System monetary and credit policy toward moderately less ease, but have been rejected by the Federal Open Market Committee. The last three meetings of the Committee offered two practical openings for a policy change, while the intervening third meeting prevented the possibility of any overt move because of impending U. S. Treasury financing and the consequent need of maintaining a relatively unchanged policy position.

The spreading weakness in the stock market that culminated in panic conditions and a collapse of prices on May 28 has thrown up a new obstacle against a change in monetary and credit policy, in that Federal Reserve System policies are a vital part and influence in the entire complex of the factors that comprise the entire financial market, and it would be unwise at this juncture to make any immediate policy change, for to do so could further unsettle financial market conditions. A calm and undisturbed Federal Reserve System policy posture is called for at the present time. However, the need for a revised policy that will produce a firmer interest rate structure is as pressing as ever, and the first opportunity for its achievement should be seized upon.

The ambivalent efforts that have been made to hold up the yields on U. S. Treasury bills as a deterrent to the movement of gold and U. S. dollars abroad at the same time that the main burden of Federal Reserve System policy actions has been on the side of credit ease have resulted in pegging U. S. Treasury bill yields. In the eyes of operators in the U. S. Government securities market, the Federal Reserve System's monetary and credit policy objectives have come increasingly into a kind of disrepute, which has had by-product effects on the markets for municipal and corporation fixed interest obligations, which are becoming progressively unsettled. In formulating Federal Reserve System monetary and credit policy, a paramount need exists for returning as quickly as possible to a free market concept, by virtue of which the interest rate structure will be freed from artificial manipulations and will develop naturally out of the uninhibited influence of the supply and demand for the use of funds available to the market.

In the interval before the next meeting of the Federal Open Market Committee any opportunity for a revision in monetary and credit policy should be exploited, even to the extent of calling a special meeting of the Committee for that purpose. By the same token, a special meeting of the Committee should be called to deal with any kind of emergency in the U. S. Government securities market that might develop in the event that the serious conditions in the stock market should be communicated to other investment areas and react in unusually heavy drains on our gold reserves.

Mr. Wayne reported that business activity in the Fifth District had continued to improve in recent weeks, probably at a somewhat faster pace than in the country as a whole. April gains in nonfarm employment and factory man-hours were quite general, and unemployment had steadily declined. The Reserve Bank's latest canvass of District business leaders suggested that most of the April increases continued into May. Durable goods manufacturing had probably not advanced beyond the good levels reached in April except in the furniture industry, which continued to show significant improvement. Reports from the textile industry presented a rather neutral picture, but respondents covering the nondurable goods group as a whole indicated that new orders, shipments, and employment had recently achieved further gains. On the other hand, coal orders and shipments had declined in recent weeks, causing some layoffs, reduced workweeks, and small price cuts. Regarding general business prospects, about three-fourths of the respondents to the Bank's periodic surveys had regularly expected either no change or only slight improvement since the first of the year.

Turning to the policy field, Mr. Wayne noted that for many months the Committee had been faced by a conflict between the requirements of the domestic and the international sectors of the economy. In recent weeks both sectors had been marked by increased uncertainty about the near future. Falling stock prices had been both a reflection and a cause of this uneasiness. The sharp decline in the trade balance for March was a contributing factor in the international sector, while on the domestic side a cautious attitude was reflected by declining forward purchase commitments by business firms, a slow drop in orders for machinery and equipment, a sluggish rise in capital outlays, and wholesale prices that were slightly on the weak side. The international situation was clearly delicate and potentially dangerous. Beyond what was already being done, however, he did not believe that monetary policy could make any significant contribution toward its improvement short of some comprehensive and drastic move which would have to be aimed at raising long-term as well as short-term interest rates. Such a move was not warranted by the domestic situation and, he believed, would be highly undersirable. Further, he did not believe that any small increase in short-term rates would have any significant effect on the balance of payments. On the domestic side, perhaps the greatest contribution the Committee could make would be to insure that no fear of any credit squeeze was added to the other uncertainties which were developing. For that reason, he believed that the Committee should continue to make available a supply of reserves sufficient to maintain a condition of moderate ease, as it had been doing for a number of weeks. He would favor renewing the current directive and leaving the discount rate unchanged.

Mr. Clay commented that although domestic economic developments had continued to show improvement in recent weeks, the pattern had been by no means uniform. It still was correct to characterize aggregate economic activity as less than vigorous. Moreover, the basic fact remained that the economy had a long distance to go in order to attain a satisfactory rate of utilization of manpower and other resources. Under the circumstances, he felt that the domestic economy continued to call for monetary policy to be expansionary with a view to fostering a higher level of economic activity. This would be reflected in a further growth of bank credit on a seasonally adjusted basis and further downward movement in interest rates.

For some time, Mr. Clay noted, the Committee had endeavored to affect favorably the international flow of funds by the general level at which it had maintained the Treasury bill rate. This action had pointed up the conflict between the Committee's current domestic and international objectives. The open market operations required to maintain the Treasury bill rate at a higher level than it otherwise would have been had tended to be restrictive in nature. The Committee had sought to avoid or reduce this effect by making purchases in other sectors of the Government securities market.

At the last meeting of the Committee, Mr. Clay recalled, it had been suggested that the relative level of interest rates in international markets throughout the maturity structure should be considered henceforth in formulating monetary policy. More specifically, the view advanced looked with favor upon a higher level of interest rates in the United States throughout the maturity range, so that these rates would be higher relative to rates in foreign markets. Clearly, this approach to the problem would involve a more restrictive monetary policy, which in his opinion would jeopardize the improvements in the domestic economy resulting from the expansionary policy that had been pursued. Moreover, there was a real question whether the increase in interest rates necessary to affect materially the international flow of funds would not be of such magnitude as to be severely restrictive in terms of monetary policy and its impact on the domestic economy.

At a time when the performance of the domestic economy was far from satisfactory, Mr. Clay thought that the question was whether monetary policy should not be directed toward providing more instead of less stimulus to the pace of activity. Certainly, as he saw it, no action should be taken to foster higher intermediate- and long-term interest rates; the downward trend of recent months had been salutary and should be encouraged to continue. The Treasury bill rate might be maintained within the same range as it had been for some months, with offsetting open market operations as necessary in order to maintain reserve availability. No change was recommended in the Federal Reserve Bank discount rate, and he felt that the directive could well be renewed in its present form.

Mr. Scanlon reported that in general business activity in the Seventh District appeared to be following the national pattern. However, home building in most District centers was below a year ago, in contrast to the strong national picture.

It appeared to him, Mr. Scanlon continued, that during the past several weeks there had been a marked difference in the attitude of consumers and the attitude of businessmen. According to the indications of recent surveys, the consumer's confidence in his financial well-being had improved, and he was now more interested in buying automobiles and other durable goods. (Of course, the behavior of the stock market in the past few days might have changed the survey indications somewhat.) As to businessmen, many of them had expressed disappointment despite the facts reported on items such as employment, the work-week, construction, and housing starts, all of which were highly encouraging. The consumer appeared to be acting on a more favorable evaluation of the economic situation.

In the Seventh District, department store sales during the four weeks after Easter were 12 per cent above a year ago, compared to a rise of 10 per cent nationally. Auto sales during the first 20 days of May maintained the advanced April level. Reflecting the trend of sales, auto assemblies during the past three weeks were at an annual rate of 8 million, the highest since December. However, estimates of Detroit sources were still based on sales of 6.8 to 7 million cars this year, including imports.

Mr. Scanlon also reported that local manufacturing output in major centers, based purely on use of electric power, showed gains in the most recent month reported, the increases from a year ago ranging from 16 to 18 per cent. Steel output had declined about 30 per cent from the March level in the District as well as nationally, and some further decline was still in prospect. Order trends were being evaluated somewhat less favorably than three weeks ago. Employment reports were moderately encouraging; unemployment compensation claims were below the levels of the past two years. Housing contracts were down 9 per cent from a year ago, compared with a rise of 18 per cent nationally. Only in Indianapolis was an increase reported. Mortgage terms in Chicago had eased only slightly since the first of the year.

As to banking developments, Mr. Scanlon reported that business loan demand was relatively strong, although not as strong as the bankers would desire. From the end of January until the middle of May, business loans had risen at a rate twice as fast as nationally. Chicago banks had regained a modest surplus reserve position since the middle of April, and the larger banks had been sellers of Federal funds. Between the middle of April and the middle of May, the banks reduced their bill holdings and purchased other securities.

Turning to policy, Mr. Scanlon commented that although most business news had been favorable during the past several weeks, demands on resources continued to be moderate. Wholesale price increases were at least balanced by price declines. One must necessarily take into account the possibility of the further development of adverse business sentiment due to the stock market, along with some dissatisfaction regarding order and profit trends. In his view, current monetary policy should be continued until the next meeting of the Committee, and he would not recommend a change in the discount rate at this time. The current policy directive might be continued unless the Committee wanted to give some recognition to the current stock market situation. If changes were made, he would like to see the phrase "short-term" eliminated from the final clause of the directive, which called for taking account of the desirability of avoiding downward pressures on short-term interest rates.

Mr. Deming reported that the most notable Ninth District economic development in the past three weeks had been a dramatic turnaround in crop prospects for 1962. From the first of April through the middle of May there had been little rain, but since then there had been a great deal of rain, and everyone was now optimistic. Otherwise, the District was continuing pretty much along the lines indicated at previous Committee meetings.

As to the coming three weeks, Mr. Deming expressed agreement with those who believed that monetary policy should not be changed. By that, he meant that there should be no change quite explicitly in terms of most of the significant guides. For example, he would not like to see the free reserve level change significantly even though the maintenance of that level might result in lower bill rates and a somewhat easier money market than had been sought in the past three weeks. In other words, he would like ot see the indicators that were watched by the public maintained without change, and he had some feeling that the Committee ought to say this in the current policy directive. For example, the first paragraph of the directive might be changed to read somewhat as follows: "In view of the continuing modest advance of economic activity and the continued underutilization of resources, and in light of recent stock market developments, but with continued recognition of the adverse balance of payments situation, it is the policy of the Federal Open Market Committee to continue in a posture essentially unchanged from that of recent weeks." Such changes in the first paragraph would reflect the Committee's awareness of stock market developments in the past three weeks, and he thought this would be desirable from the standpoint of the record. He would recommend no change in the discount rate at this time.

Mr. Swan reported that the Twelfth District, like the nation, showed some further, but very moderate improvement in the business situation in April. According to scattered indicators, the same trend continued into early May. There had been a slight reduction in the rate of unemployment, the seasonally adjusted rate having fallen from 5.8 per cent in March to 5.7 per cent in April. Lumber markets in the District had firmed somewhat as new orders exceeded production, and western steel production had declined much less than the decline for the country as a whole. In the three weeks ended May 16, District weekly reporting banks reflected gains in loans, including a marked increase in real estate loans. As a general statement, there did not appear to be any very significant differences between the District situation and the over-all picture for the country.

In terms of policy, Mr. Swan said it seemed to him that the Committee should maintain much the same position that it had maintained quite recently. Since the economic upswing certainly was not vigorous and further uncertainties had been introduced by stock market developments, he did not think that any significant change in policy would be desirable. Like Mr. Deming, he felt that a continuation of policy without change should be related to the free reserve level, which for the immediate future should be held about where it had been, that is, $450 million or thereabouts. If this meant some decline in the bill rate below 2-3/4 per cent, no attempt should be made to offset that decline by a significant reduction in free reserves.

As to the current policy directive, Mr. Swan concurred with the view of Mr. Hayes that it was not desirable to have the directive remain unchanged for a lengthy period, particularly in light of current developments. Therefore, he would like to see those developments recognized in the first paragraph. In the second paragraph, he was bothered by the phrase that called for avoiding sustained downward pressures on short-term rates. While there could be different interpretations of the word "sustained," it might be argued that any reduction below 2-3/4 per cent in the bill rate would be regarded as reflecting sustained pressure. Accordingly, he would favor eliminating that particular phrase. He would not recommend changing the discount rate at this time.

Mr. Irons reported that economic activity in the Eleventh District was proceeding favorably. There was strength in the employment picture, with total nonagricultural employment moving to a near record and unemployment, on an unadjusted basis, falling to about 4.3 per cent of the labor force. The trend of consumer demand was favorable. Industrial output was up, and construction was up sharply. Except for some developing dryness, which was not a great problem, the agricultural situation was quite good. In summary, economic activity was proceeding at a moderate upward pace.

Mr. Irons also said that Eleventh District banks seemed to be adequately liquid. There had been increased loan demand in the past three weeks, especially for business and construction loans, with a reduction in investments. Demand deposits were off a bit, and savings deposits were up a little. The growth of savings deposits was slowing down. There seemed to be little change in the demand for Federal funds, with purchases running at an average of about $500 million and sales about $450 million. Except for some small amount of seasonal borrowing, there was little activity at the discount window.

Turning to policy, Mr. Irons commented that when he left Dallas for this meeting he had in mind some tentative conclusions. It seemed to him that the System had done about as much in the way of supplying reserves as would be appropriate under the circumstances, and he leaned toward a somewhat less generous approach to the providing of reserves, even though that might result in some firming of interest rates. However, the events of the past few days had changed his line of reasoning. The economic statistics looked quite good, but attitudes, the confidence factor, and related matters were less favorable and the developments in the stock market could not be ignored. Accordingly, he concluded that this was a good time to maintain the status quo, while reexamining the System's position, evaluating the consequences of what was going on in the stock market, and appraising the matter of business confidence. Perhaps another look should be taken at economic trends to see whether any factors were developing of which the Committee had not been aware. In particular, he would want to watch consumer reaction--and also the international reaction--to the recent stock market developments. There were a lot of unanswered questions that were being brought to the fore by the financial market changes. Thus, the situation seemed to call for study of possible consequences rather than for action at this moment.

In summary, Mr. Irons said, his views were much the same as those expressed by Mr. Robertson. He would maintain the status quo as nearly as possible and avoid overt action of any kind at this time. He would not change the discount rate or the current policy directive.

Mr. Ellis reported that New England business conditions had shown continued modest improvement since the previous meeting of the Committee. No sector of the economy showed signs of disturbing weakness, and no sector showed signs of unsustainable expansion. Most manufacturing industries strengthened in April, and man-hour data suggested a rise in the index of production. Nonmanufacturing employment seemed to have been a little weaker in April than seasonal expectations.

Mr. Ellis also reported that First District reporting banks found business loan demand just about meeting seasonal expectations.

Total loans and investments continued to grow at a good pace. The growth of deposits was holding loan-deposit ratios fairly stable. District banks had been fairly heavy net sellers of Federal funds in the past five weeks.

Turning to policy, Mr. Ellis commented that he, like some others, had left for this meeting prepared to urge a change in the policy guidelines. After the stock market events of yesterday, however, he had shifted to a position of no change in policy at this time. As to what no change in policy might mean, he noted that there are several anchors of policy, among them free reserves, avoidance of sustained downward pressures on short-term rates, and concern with financial markets in general. The question was to which anchors of policy the Committee desired to cling most strongly in the next few weeks. According to the projections, the System was going to have to inject several hundred million dollars of reserves in the next two weeks. He would urge that they not be injected in a way that would promote further pressure on short-term rates, for he would not want to give up the objective of avoiding that kind of pressure. His definition of no change in policy would be no change from the weeks in April rather than the most recent three-week period, which was characterized by greater ease in the money market centers, traceable perhaps in some degree to Treasury operations.

Mr. Ellis said that he would like to see the Committee recognize changes in the economic situation in the first paragraph of the current policy directive. One of the purposes of instituting the present procedure was to be able to recognize such changes, and he felt that the Committee's record of understanding and evaluating the situation it was attempting to meet would read better if there was some recognition of the changes that had occurred since March. The language suggested by Mr. Deming would go some way in that direction. Mr. Deming, however, had omitted the phrase that called for promoting further expansion of bank credit and the money supply. He (Mr. Ellis) would like to see that phrase retained, but to have the word "promote" changed to "permit," as suggested by Mr. Shepardson at the May 8 meeting.

Mr. Balderston said that he would advocate holding just as steady as possible. However, he was impressed by the reasons for changing the wording of the current policy directive. His suggestion would be to eliminate the second paragraph and change the first paragraph somewhat as follows: In view of the continued under-utilization of resources, the modest rate of domestic expansion, and the recent sharp decline in stock market prices, the Federal Open Market Committee is continuing its policy of promoting the expansion of bank credit and the money supply.

In discussion of his proposal, Mr. Balderston said the sharp decline in stock market prices, along with the results that might flow therefrom, constituted the principal reason why he would continue present policy. Otherwise, he might be inclined to veer toward less ease. His proposed directive would make no reference to the international situation because he had a feeling that the Committee had been "driving on both sides of the road long enough" and as a result its directives were not clear. He would drop the second paragraph of the present directive because it seemed to him that it was redundant.

Mr. Francis commented that Eighth District business conditions continued to improve to about the same extent as indicated by many of the other District reports that had been given.

Chairman Martin noted from a news ticker report that had been brought to him that stock market prices had experienced another substantial decline this morning. He went on to say that before this meeting he had attended a meeting at the White House with the President and other officials of the Administration. He felt constrained to say to the Committee that the President throught the Federal Reserve System, like the rest of the Government, had an obligation in this matter. Against this background, he told the President that the Board of Governors had discussed yesterday the question of margin requirements, at which time the Board members were of the view that "steady in the boat" was the proper course. The President's position was that the Federal Reserve should follow whatever course it thought would be most helpful; he raised the question whether, if the Board was not going to change the margin requirements, it would be desirable for the Board to say that it was not going to change them. He (Chairman Martin) left with the President, as a matter of general information, a paper on the pros and cons of a margin requirement change that had been prepared by the Board's staff.

Chairman Martin said he had made no commitment other than to bring to this meeting of the Committee the President's view that this was a serious situation. The President had left to the discretion of the Federal Reserve the question whether any action should be taken by the System, indicating that the System ought to do whatever it considered wisest in the present circumstances. If it was the view of the Federal Reserve that it would be better not to issue any statement, that was for the System to decide. If, on the other hand, there was a feeling that the System should make a statement, the President would be glad to have such a statement made.

The Chairman then read from a news ticker report the answers that had been given this morning by Secretary of the Treasury Dillon to questions raised by reporters. Mr. Dillon reportedly attributed to the White House conferees a feeling that stock prices had been on the high side and had now dropped to a level more in keeping with price-earnings ratios. Mr. Dillon stressed that the Government had no controls directly affecting stock market prices. He also pointed out that margin requirements were a matter within the sole discretion of the Board of Governors. Mr. Dillon urged speedy Congressional action on the proposal to allow tax credit to businesses on purchases of equipment. He did not feel that the stock market developments reflected any decline in confidence outside the stock market. He noted that stock prices had already started on a downward trend before the steel price episode.

Chairman Martin then said that he would like to indicate to the Committee his own thinking on monetary policy, which was much along the lines that some members of the Committee had expressed prior to the recent stock market decline. His view was, in essence, that the System had gone as far as it should with a policy of easy money and that such a policy had outlived its usefulness. This did not mean, however, that the System should take any overt action at this particular time. On the basis of his recent visit abroad and the views expressed by people with whom he had been talking recently, he felt there was something more fundamental in the stock market situation than easy money. Unquestionably, however, the developments in the market reflected the backwash of speculation in a wholesale manner that had been going on all around the country. The margin requirements, he thought, had been reasonably effective in controlling the amount of credit going into speculation in stocks, but they had not affected real estate and other speculative activities. Therefore, he was inclined to feel that easy money was part of the total picture; he doubted very much whether it could be said that easy money had nothing to do with the situation. While he felt that the Federal Reserve had been thoroughly justified in the course it had been pursuing, the System could not just go along thinking that easy money was going to produce an exuberant economy.

Continuing, Chairman Martin said that he would like to reiterate a view he had expressed a number of times before, namely, that the balance of payments problem overshadowed everything else. He would not want to say that this was the crisis he had referred to several times as a possibility, but the situation conceivably could develop such proportions.

As to policy for the immediate future, the Chairman said it was his feeling, on the basis of the discussion at this meeting, that the wisest course would be to stay steady in the boat and make no change in policy of any sort at this moment, but rather to continue to evaluate the problem. Whether there should be a change in the current policy directive along the lines that had been suggested or whether it would be wiser to renew the directive in its present form was open to debate. However, it seemed that the majority sentiment was clearly for no change in policy at this particular time.

Chairman Martin inquired whether there were any questions about the accuracy of his statement of the consensus as to policy for the immediate future, and no such question was indicated.

There followed, however, consideration of the wording of the current economic policy directive in light of the several suggestions that had been made, and it was the prevailing view that some reference to recent developments in the stock market should appropriately be incorporated in order to place on record that this was a factor recognized by the Committee in shaping its policy for the forthcoming period. Certain other possible changes in the directive, such as to provide for "permitting" rather than "promoting" further expansion of bank credit and the money supply, were decided against in view of the basic decision of the Committee to continue monetary policy unchanged at this time.

At the conclusion of this discussion, there was read to the Committee language for the first paragraph of the directive reflecting a formulation with which there appeared to be general agreement, and the expressions of the Committee members were favorable.

Accordingly, upon motion duly made and seconded, the Federal Reserve Bank of New York was authorized and directed, until otherwise directed by the Committee, to execute transactions in the System Open Market Account in accordance with the following current economic policy directive:

In view of the modest nature of recent advances in the pace of economic activity, the continued underutilization of resources, and the uncertainties created by the disturbed conditions in some financial markets, it remains the current policy of the Federal Open Market Committee to promote further expansion of bank credit and the money supply, while giving recognition to the country's adverse balance of payments.

To implement this policy, operations for the System Open Market Account during the next three weeks shall be conducted with a view to maintaining a supply of reserves adequate for further credit and monetary expansion, taking account of the desirability of avoiding sustained downward pressures on short-term interest rates.

Votes for this action: Messrs. Martin, Hayes, Balderston, Bryan, Deming, Ellis, Fulton, King, Mills, Mitchell, Robertson, and Shepardson. Votes against this action: None.

Chairman Martin said he wished to place on record at this point that he had told the President of the United States this morning that the Presidents of the Federal Reserve Banks and the members of the Board of Governors might be counted upon to do whatever they could, regardless of whether any statement was issued by the Federal Reserve System, to maintain a sense of order in the present situation. He did not say to the President that any particular course of action would be taken by the Federal Reserve System, but he did say, as he had indicated, that the President could count on all of the Reserve Bank Presidents and members of the Board of Governors to do whatever was possible to maintain balance. The President, in turn, expressed his desire that those in the Federal Reserve bend their best efforts in that direction.

General agreement was expressed as to the appropriateness of the comment that the Chairman had made to the President. Question was raised, however, as to what kind of statement the President might have in mind that the Federal Reserve could issue.

Chairman Martin responded to the effect that there had been no effort by the President to press the Federal Reserve System to do anything that it did not want to do. The President was approaching the current problem entirely from the standpoint of his responsibility as Chief Executive. The President did say that if he were doing it himself, he would be inclined to reduce margin requirements, in which connection he noted that this was the only selective credit control available. In turn, Chairman Martin said, he indicated to the President that there was a question whether the Board would feel that a reduction in margin requirements at this time was advisable. However, he had told the President that he would relay the latter's comments to the Board. The President then suggested that if the Board was not going to change margin requirements, it might be helpful for the Board to issue a statement to such effect and give the reasons.

Chairman Martin emphasized that he regarded his conference at the White House as entirely satisfactory. More specifically in response to the question that had been raised, Chairman Martin said he did not think that any of those who had conferred at the White House had in mind exactly what kind of a statement by the Federal Reserve might be helpful. Personally, he was less inclined toward the issuance of statements than some others might be; he felt there could be too many statements.

There followed discussion with respect to the possible public reaction to any statement that might be issued by the Federal Reserve, including a statement that the Board did not intend to reduce margin requirements.

The Chairman then repeated that in his view there was something more fundamental in the stock market decline than the level of margin requirements. He had been concerned for some time about the fact that a number of foreigners with whom he had talked seemed to feel that the post-war cyclical peak of the Western economies was being reached. Therefore, they were inclined to be rather bearish about their own countries as well as the United States. In this connection, Chairman Martin noted that substantial price declines were occurring on the European stock exchanges; the downward movement in stock prices was fairly general and was not limited to this country.

Chairman Martin commented further that he did not know what type of statement might be issued by the Federal Reserve that would be helpful. In any event, however, this was clearly not a situation where a statement could be drafted by a number of people sitting around the table, as at this meeting. He thought the comments that had been made to the press yesterday and today by the Chairman of the Council of Economic Advisers and by the Secretary of the Treasury were essentially correct. On the basis of the reports made during the go-around at this meeting, there was nothing that would lead him to think that there should logically be general dumping of stocks at current prices.

In further discussion, Mr. Mills suggested that in view of the uncertain nature of future developments the Open Market Committee might want to consider authorizing Chairman Martin to issue a statement if, in his judgment, such a statement should seem desirable, with the understanding that the choice of words therein would be left to Chairman Martin and any person or persons with whom he might want to consult.

The comments that ensued indicated that the members of the Committee found it difficult to envisage any type of Federal Reserve statement that might be helpful in the present situation. At the same time, it was recognized that some turn of events might produce a situation wherein the issuance of a statement would seem desirable. Against this possibility, members of the Committee indicated that they would be agreeable to giving an authorization to Chairman Martin along the lines that had been suggested by Mr. Mills.

Chairman Martin commented that this was not a responsibility he was particularly seeking. Yet it was hard to envisage what might develop within the next week or ten days.

It was then moved by Mr. Shepardson and seconded by Mr. Hayes that Chairman Martin be authorized, during the period until the next meeting of the Open Market Committee, to issue a statement on behalf of the Committee with regard to stock market developments and related economic or financial developments if events should occur that in his judgment made it desirable to issue such a statement.

> This motion was carried by unanimous vote, subject to the understanding that in certain circumstances Chairman Martin might deem it advisable to call a special meeting of the Open Market Committee before the next regular meeting of the Committee, scheduled for Tuesday, June 19, 1962.

Under date of December 11, 1961, there had been transmitted to the Committee members and other Reserve Bank Presidents a draft revision of the 1957 Federal Open Market Committee Guides for Emergency Operations with a request for comments. The Open Market Committee Guides had been reviewed pursuant to a suggestion made when the Board of Governors approved revised Guidelines for Emergency Monetary Policy as of May 15, 1961. In light of comments received following distribution of the preliminary draft revision of the Open Market Committee Guides, a revised draft was distributed by the Secretary of the Committee under date of May 17, 1962.

> Upon motion duly made and seconded, and by unanimous vote, the revised Federal Open Market Committee Guides for Emergency Operations, in the form distributed with the Secretary's memorandum of May 17, 1962, were approved.

Mr. Williams then withdrew from the meeting.

There had been distributed to the Committee a report from the Special Manager of the System Open Market Account on System and Treasury operations in foreign currencies and on foreign exchange market conditions for the period May 8 through May 23, 1962, along with a supplementary report for the period May 24 through May 28, 1962. Copies of these reports have been placed in the files of the Federal Open Market Committee.

As indicated in those reports, there had been no System foreign currency transactions during the period since the Open Market Committee meeting on May 8, 1962. Accordingly, no action to approve, ratify, and confirm any such transactions was necessary.

At the request of the Chairman, Mr. Coombs presented comments in supplementation of the aforementioned written reports, in the course of which he referred to certain documents that had been distributed to the Committee with respect to a possible dollar-sterling swap arrangement. The first memorandum, dated May 16, 1962, described a meeting in London on Monday, May 7, in which Mr. Coombs, Mr. Roosa, Under Secretary of the Treasury for Monetary Affairs, and representatives of the British Treasury and the Bank of England participated. As the result of this meeting a telephone call had been received by Mr. Coombs on Tuesday, May 15, from an official of the Bank of England who informed him that the British financial authorities were agreeable to a $50 million swap at flat rates and an identical interest rate, which might be set at 2 per cent. In connection with this swap possibility, there had also been distributed a memorandum from the Secretary of the Committee dated May 25, 1962, with respect to recent economic developments in the United Kingdom. In this memorandum the view was expressed that the economic outlook in the United Kingdom would justify the holding by the System of pounds sterling under a swap agreement with the Bank of England.

Further, with a transmittal memorandum dated May 28, 1962, there had been distributed to the Committee a copy of a cable from Mr. Coombs to the Bank of England dated May 18, 1962, suggesting the text of a press release that might be used in event of the completion of a dollar-sterling swap arrangement, along with a copy of a cable sent to the Bank of England by Mr. Coombs on May 21, 1962, outlining the proposed terms of such an arrangement. The draft proposal was for a sterling-dollar swap in the amount of $50 million, the swap to have a maturity of three months and to be liquidated on date of maturity at the original rate of exchange. The Bank of England would place the resultant dollar balance in a nontransferable U. S. Treasury certificate of indebtedness which would be issued by the U. S. Treasury at par to mature three months after date of issue, but redeemable upon two days' notice, and which would bear interest at the rate of 2 per cent per annum. The sterling balance accruing to the Federal Reserve System would bear the same rate of interest. The swap arrangement, including the U. S. certificate of indebtedness, would be renewable upon agreement of both parties. To protect both parties against the remote risk of a revaluation of either currency, the Federal Reserve would place with the Bank of England a standing order, to be executed when necessary for that purpose, to purchase for Federal Reserve account sterling in any amount sufficient to replenish any earlier drafts upon Federal Reserve sterling balances created by the swap. The Federal Reserve would accept from the Bank of England a similar standing order.

Mr. Coombs recommended that the Federal Open Market Committee approve a dollar-sterling swap arrangement on the terms outlined in the cable of May 21, 1962, effective May 31, 1962, in which connection he stated reasons for believing that such an arrangement would be advantageous.

Mr. Robertson stated that he continued to be skeptical about the whole program of System foreign currency operations. However, inasmuch as the program had been initiated, he would be willing to vote to approve the proposed dollar-sterling swap arrangement.

Inquiry was made about the desirability of issuing a press release, and Mr. Coombs commented that it was his impression that the announcement of arrangements of this kind had a stabilizing influence on the exchange markets. The reaction conceivably might be different in present circumstances, but the record had been favorable thus far.

Chairman Martin indicated that he would be apprehensive about the result if such an arrangement were entered into without a press release being issued and knowledge of the arrangement nevertheless became known.

Other members of the Committee expressed agreement with the views stated by Chairman Martin and Mr. Coombs.

> Thereupon, the proposed dollar-sterling swap arrangement was unanimously approved effective May 31, 1962, with the understanding that a press release would be issued along the lines set forth in Mr. Coombs' cable of May 18, 1962.

Mr. Coombs next referred to his memorandum, distributed to the Committee under date of May 21, 1962, regarding the possibility of a dollar-guilder swap arrangement with the Netherlands Bank, which might involve a pilot swap of $10 million plus a standby swap of $40 million. The memorandum pointed out, among other things, that the Netherlands Bank would be unable to place any Federal Reserve holdings of guilders in either commercial paper or a time deposit. However, it was thought probable that the Federal Reserve could obtain a guilder time deposit facility at the Bank for International Settlements. With this exception, the suggested swap arrangement would be along the lines of the arrangement with the Bank of France. One immediate objective would be to mop up as much as possible of the prospective flow of dollars into the Netherlands when, on June 27, 1962, the Dutch Philips Corporation was to receive payment on subscriptions for a new stock issue that might yield roughly $200 million equivalent. An estimated $80 million might be raised from United States subscribers, with a $50 million inflow in prospect from subscriptions in other European countries. Since it was the traditional policy of the Netherlands Bank to convert into gold all dollar and other foreign exchange acquisitions in excess of $200 million, and since present dollar holdings of the Bank amounted to around $183 million, the dollar receipts generated by the Philips issue would mean that the Netherlands Bank would shortly be compelled to make heavy purchases of gold from the United States.

In connection with the possible reciprocal transaction between the Federal Reserve and the Netherlands Bank, there had also been distributed a memorandum from the Secretary of the Committee dated May 25, 1962, which discussed recent economic developments in the Netherlands and expressed the view that the immediate economic outlook would justify the System's holding of guilders under such an agreement with the Netherlands Bank. In a memorandum from the Committee's General Counsel dated May 28, 1962, concerning the legal aspects of several proposed swap arrangements with foreign banks, the view was expressed that there would be no legal objection to placing Federal Reserve guilder holdings in a time deposit with the Bank for International Settlements.

In comments supplementing his memorandum, Mr. Coombs noted that the possible swap arrangement would extend the dollar defense line to another important European currency and provide the possibility of mopping up the flow of dollars into the Netherlands Bank as payment was made for the Philips issue. The Netherlands Bank was agreeable to the swap in principle. The main technical problem was the inability of the Netherlands Bank to place Federal Reserve holdings of guilders in either commercial paper or a time deposit. Therefore, Mr. Coombs had been talking not only with the Netherlands Bank but also with the Bank for International Settlements about the possibility of a time deposit facility. Yesterday, word was received of agreement in principle on the part of both the Netherlands Bank and the Bank for International Settlements that such a time deposit facility would be feasible. The Federal Reserve would be able to obtain a rate of interest thereon equivalent to the rate made available to the Netherlands Bank on its holdings of dollars. In this case, Mr. Coombs felt, it might be useful to follow the pattern of the French swap and to base the interest rate upon the last Treasury bill issue immediately preceding the swap. He would regard the 2 per cent rate of interest in the proposed dollar-sterling swap as a deviation from the general pattern. The deposit with the Bank for International Settlements would be a three-month time deposit subject to withdrawal on two days' notice.

In response to a request from Mr. Mitchell for further elaboration of the reasons for the swap arrangement, Mr. Coombs said the Netherlands had been running more or less in even balance in international payments for the past year. However, the payment for the Philips issue would involve a substantial influx of funds. The question was whether it would not be useful to try to deter the prospective drain on U. S. gold reserves. Before the expiration of three or six months, the guilder might come under some selling pressure; the Netherlands was not in a strong surplus position. The worst that could happen was that the United States would eventually lose as much gold as if there were no swap arrangement in effect.

With regard to the traditional policy of the Netherlands Bank to convert into gold dollar and other foreign exchange acquisitions in excess of $200 million, Mr. Swan inquired whether, if the swap arrangement were entered into, there was reason to believe that the Bank might be induced to alter its policy.

Mr. Coombs replied that he thought the consummation of a swap arrangement might have such an effect. The Swiss, as a quid pro quo for Stabilization Fund forward operations, had let their dollar balances run up, and the same sort of development could occur here. He did not think that a swap arrangement would lessen the possibility of the Netherlands Bank considering some adjustment of its traditional policy.

After further discussion had indicated that the Open Market Committee was inclined to look with favor on a proposed dollar-guilder swap arrangement such as described, Mr. Coombs asked whether he understood that the Committee would prefer to authorize the negotiation of such a swap or to approve in principle. He would hope the latter, with the possibility of obtaining final approval of the arrangement by poll of the Committee. If possible, he would like to move forward on this matter before the next Committee meeting.

> Thereupon, unanimous approval was given in principle to a dollar-guilder swap arrangement with the Netherlands Bank along the lines described in Mr. Coombs' memorandum of May 21, 1962, it being understood that the arrangement was subject to final approval by the Federal Open Market Committee.

Mr. Coombs then referred to his memorandum, distributed to the Committee under date of May 23, 1962, with regard to possible Belgian franc operations. Attached to the memorandum was a letter from the National Bank of Belgium suggesting a swap arrangement in the amount of $50 million for six months, renewable, with an identical interest rate on both sides. The dollars accruing to the National Bank of Belgium would be invested in special U. S. Treasury certificates of indebtedness, while the Belgian francs accruing to the Federal Reserve would be invested in bills (promissory notes) issued by the National Society of Credit and Industry. The U. S. certificates and the Belgian bills would be issued for six months, but would be redeemable or discountable at any time, on demand, at par value and without modification of interest. The interest rate would be 2.75 per cent on both sides.

In a memorandum from the Committee's General Counsel dated May 28, 1962, question was raised whether investment of Belgian francs in notes of a Belgian company engaged in providing credit for commerce and industry would be clearly authorized. However, the question was understood to have become academic. As stated in Mr. Coombs' memorandum of May 23, he had inquired of the National Bank of Belgium whether it would be possible to place Federal Reserve holdings of Belgian francs on time deposit with the Bank for International Settlements. The offhand reaction was that this might prove feasible, and a definite answer was promised as soon as possible.

In connection with the swap possibility, there had also been distributed a memorandum from the Secretary of the Committee dated May 25, 1962, regarding recent economic developments in Belgium in which the view was expressed that the immediate economic outlook seemed more favorable than for some time and that it would justify the holding of Belgian francs under a swap agreement with the National Bank of Belgium.

In supplementary comments on this swap possibility, Mr. Coombs noted that it would provide still another link in the line of bilateral exchange arrangements. He thought it would be possible to work out the procedure whereby Belgian franc holdings of the Federal Reserve System would be placed on time deposit with the Bank for International Settlements. He would recommend approval of a dollar-Belgian franc swap in principle, in the amount of $50 million.

In response to a question as to why this swap arrangement was proposed on a six-month basis, Mr. Coombs said he thought this was intended to be something of a generous gesture on the part of the National Bank of Belgium. The letter from the National Bank might be regarded as an indication of what that Bank would be willing to consider. However, he would prefer a three-month swap on a renewable basis to keep the arrangement more in line with the other swap arrangements negotiated or pending, and that was what he would suggest.

Question was raised as to whether a swap in the amount of $50 million with the Belgians would not be out of line in terms of the arrangements with other countries, whether $50 million was looked upon as a minimum for swap arrangements, or whether there were particular reasons for that figure in the case of the proposed transaction with the National Bank of Belgium.

Mr. Coombs replied that the Belgians had suggested $50 million. Perhaps they had taken into account their policy of converting into gold practically all of their dollar inflow and thought of the $50 million figure as a gesture of cooperation from that standpoint. Mr. Coombs said he would agree that swap arrangements of $50 million all around, regardless of the size of the country concerned and the balance of trade, might seem somewhat illogical. In time, he thought, there might be higher figures with the United Kingdom and France than with other countries.

> Thereupon, unanimous approval was given in principle to a dollar-Belgian franc swap arrangement with the National Bank of Belgium along the lines described in the letter from the National Bank of Belgium dated May 16, 1962, and Mr. Coombs' memorandum of May 23, 1962, it being understood that the arrangement was subject to final approval by the Federal Open Market Committee.

Mr. Coombs next referred to his memorandum, distributed to the Committee under date of May 22, 1962, with respect to a possible swap arrangement with the National Bank of Switzerland. This involved the possibility of a medium-term credit arrangement. In conversations with Mr. Coombs in Europe, officials of the National Bank of Switzerland had indicated that the Bank would expect to provide credit under a swap arrangement on a 90-day basis, but with a tacit understanding that the credit would be renewed for as long as might prove necessary. The Bank needed protection only against some emergency situation in which the credit facility might advisedly be shifted to a medium-term basis, and it anticipated working out some arrangement with the Swiss Treasury whereby the latter would take over the credit in such circumstances. Mr. Coombs had suggested, in the alternative, consideration of a relatively short-term swap, say for three months, with the possibility of two renewals.

The question whether a medium-term credit arrangment with the National Bank of Switzerland would be legally warranted was discussed briefly in the memorandum from Mr. Hackley dated May 28, 1962, referred to previously in these minutes. That memorandum pointed out that there was no statutory restriction upon the length or maturity of accounts that might be maintained by a Reserve Bank with a foreign bank. If it could be established that a medium-term swap arrangement was necessary or desirable in order to effectuate open market transactions in foreign currencies, Mr. Hackley felt it would be subject to no greater legal objection than a short-term, 90-day swap. However, the length of the commitment might make it more difficult, as a matter of degree, to establish that the arrangement was related to the effective conduct of open market operations. Also, an arrangement of this kind might be subject to question on policy grounds.

In comments supplementing his memorandum, Mr. Coombs noted that the U. S. Treasury was not in a position to provide a medium-term credit facility to the Swiss. Further, as Mr. Hackley's memorandum suggested, it might be difficult to establish that a medium-term credit facility provided by the Federal Reserve could be related effectively to the conduct of open market transactions in foreign exchange. His own view was that it would be preferable to keep such an arrangement on a short-term basis if possible. Therefore, he had suggested to the Swiss that they consider a swap arrangement on a 90-day basis, with the explicit understanding that the arrangement could be renewed for another three or six months. A short-term arrangement would not fully satisfy the apparent desire on the part of the Swiss more or less to match the standby credit facilities being provided by certain member countries of the International Monetary Fund. In terms of realities, however, an arrangement running for nine months might give the United States time to counter any heavy flow of speculative funds to Zurich, and possibly to bring about a reversal.

Mr. Coombs then suggested that the Committee might want to authorize further negotiations with the National Bank of Switzerland for a short-term swap facility of $150 million, with $50 million as a pilot swap and the remaining $100 million put on a standby basis. If current disturbances in the stock exchanges continued, there could be a rather heavy flow of funds to Switzerland and there might well be a need for the full $150 million.

In response to a request for further explanation of the basis for the Swiss suggestion for a medium-term credit arrangement, Mr. Coombs brought out that an important second line of defense was being established by the enlargement of the standby resources of the International Monetary Fund. If the dollar should get into serious difficulty, the United States could go to the Fund and pick up a sizable supply of European currencies. However, since Switzerland was not a member, the Fund arrangement did not cover the Swiss franc, and the Swiss felt a certain moral obligation to do as much as they could to close the gap. They would like to work out a facility as similar as possible to those being extended by a number of the major countries in connection with the enlargement of the standby resources of the Fund, and those facilities were on a medium-term basis. The Swiss appeared to feel that a short-term arrangement might be criticized on the ground that Switzerland was failing to do its part. Mr. Coombs said he had suggested to the Swiss officials that it should be possible to provide a satisfactory explanation by tying in a short-term dollar-Swiss franc swap arrangement with the swap arrangements being negotiated with other central banks. If the swap was in terms of a figure such as $150 million, the Swiss would certainly get credit on that score.

Question was raised whether a $150 million swap would appear adequate, and also as to the relationship between that figure and the part that the Swiss might have been expected to play in enlarging the standby resources of the Monetary Fund had Switzerland been a member of the Fund.

Mr. Coombs replied that such questions were difficult to answer. He thought that the Swiss might be ready to put up as much as $250 million on a medium-term basis. Further, unless there were basic changes in underlying conditions, he foresaw the possibility of a sizable net flow of capital to Switzerland. Conceivably, of course, the situation would turn in the other direction.

> Thereupon, the Open Market Committee authorized further negotiations with the National Bank of Switzerland looking toward the possibility of a dollar-Swiss franc short-term swap arrangement along the lines described by Mr. Coombs.

Mr. Coombs then pointed out that the swap arrangement with the Bank of France in the amount of $50 million, which became effective March 1, 1962, would mature June 1, 1962. He recommended renewal of the arrangement for another three months; it was his understanding that the Bank of France was agreeable to such an extension.

In this connection, Mr. Coombs commented that the French had been taking in so many dollars during the past three months that no useful opportunity had presented itself for employment of the French francs obtained by the Federal Reserve under the swap arrangement. The entire $50 million could have been exhausted quickly. Therefore, it had seemed better to wait for a time when use of French francs might bring the market into better balance. If the heavy flow of dollars into France should continue during the summer months, it might prove desirable to liquidate the swap arrangement in advance of the next maturity, say on August 1, and then to renegotiate an arrangement in the fall months when the French payments position might be less strong.

In discussion, question was raised whether, in the circumstances described by Mr. Coombs, the amount of the swap with the Bank of France should not be raised or the arrangement dropped.

Comments made in response by Messrs. Hayes and Coombs were to the effect that in conditions such as had existed recently the use of the French francs to the extent of $50 million would have had little or no effect. On the other hand, the existence of the arrangement and lack of use of the French francs did not appear to have created any adverse reaction. In the fall months an opportunity might come. As to increasing the amount of the swap arrangement, other negotiations were now in process between the United States and France, having to do with a possible advance debt repayment and adjustments with respect to military procurement. In the circumstances, it seemed doubtful whether this was an appropriate time to suggest an increase in the terms of the swap arrangement, although that might become appropriate in the fall.

> Thereupon, the Open Market Committee approved unanimously a three-month renewal, effective June 1, 1962, of the existing dollar-French franc swap arrangement with the Bank of France.

Mr. Coombs next commented upon discussions that had been held with the Bank of Canada regarding the possibility of a swap facility involving that Bank and the U. S. Treasury. However, it had developed that the Treasury could not commit more than $25 or $30 million out of the Stabilization Fund at the present time. The reaction of the Bank of Canada was one of appreciation that this had been suggested as a token of cooperation, but the Canadians were doubtful that an arrangement of such magnitude would have much impact. It appeared that they might be interested in a swap arrangement in a much larger figure, such as $200 or $250 million, as a backstop to the recent action in establishing a par value for the Canadian dollar.

Mr. Coombs raised the question whether the Open Market Committee would be interested in exploration of the possibility of a swap arrangement between the Federal Reserve and the Bank of Canada, having in mind that the Canadians might be interested only in an arrangement of substantial size. He noted that the establishment of a par value for the Canadian dollar had been a long-sought objective of American policy. That having been done, it appeared appropriate to give some support to the Canadians. He was not sure, however, whether this might best be done through a Federal Reserve-Bank of Canada swap arrangement or through a Canadian drawing on the Monetary Fund.

In discussion, it was noted that a Canadian drawing on the Monetary Fund would subject the Canadians to the discipline of the Fund. It was also noted, however, that the Canadians might hesitate to go to the Monetary Fund until after the forthcoming elections and that they had been subjected to a speculative outflow of funds of rather substantial proportions during the past two or three months.

Mr. Mitchell raised the question whether, if the endeavor of U. S. foreign exchange transactions was to help build a strong international payments system, it would not seem almost unavoidable, in the interest of consistency, to consider a swap arrangement with the Bank of Canada.

Mr. Coombs said he had such a feeling. That was why he had favored the Stabilization Fund arrangement on a $25 or $30 million basis, but that figure apparently was not high enough in the eyes of the Canadians to have any real impact.

After Mr. Mitchell had suggested the possibility of negotiating with the Bank of Canada in terms of a swap of $50 or $100 million, Mr. Hayes said he shared the view that, with the Canadian economy so close to that of the United States and the Canadian currency so important to the United States, it would seem somewhat illogical not to include the Canadians in the network of swap arrangements at such time as a favorable basis for such an arrangement could be found.

Mr. Balderston said he also shared that view. He saw virtue in taking the initiative in discussions with the Bank of Canada, so as to be able to suggest limits compatible with the Federal Reserve swap arrangements negotiated or pending with other central banks.

> Thereupon, the Open Market Committee authorized negotiations with the Bank of Canada looking toward the possibility of a swap arrangement between the Federal Reserve and that Bank.

Mr. Coombs pointed out that on the exchange markets the United States dollar had been under considerable pressure in the past few days. It had been driven to the floor against the Swiss franc, and it was weakening against the German mark. Assuming that the German Federal Bank was prepared to intervene and buy dollars to check a further decline of the dollar rate against the German mark, he hoped that the Open Market Committee would concur in the appropriateness of using some of the Federal Reserve holdings of German marks to reinforce that operation. It seemed quite clear that a speculative movement of a reversible type was occurring, and use of the System holdings of German marks would appear to meet the criteria for intervention as stated in the Guidelines for System Foreign Currency Operations.

> The proposed use of Federal Reserve System holdings of German marks in the manner described by Mr. Coombs, if that should seem desirable to him in the light of developments, was noted without objection.

With reference to the earlier discussion concerning a possible swap arrangement with the National Bank of Belgium, it was brought out that the continuing authority directive to the Federal Reserve Bank of

New York with respect to System foreign currency operations, originally adopted by the Committee on February 13, 1962, and reaffirmed on March 6, 1962, did not authorize the purchase and sale of Belgian francs.

Accordingly, upon motion duly made and seconded, and by unanimous vote, the continuing authority directive to the Federal Reserve Bank of New York with respect to System foreign currency operations was approved in the following amended form, effective immediately:

The Federal Reserve Bank of New York is authorized and directed to purchase and sell through spot transactions any or all of the following currencies in accordance with the Guidelines on System Foreign Currency Operations issued by the Federal Open Market Committee on February 13, 1962:

Pounds sterling
French francs
German marks
Italian lire
Netherlands guilders
Swiss francs
Belgian francs

Total foreign currencies held at any one time shall not exceed $500 million.

Mr. Mitchell commented that the recent developments in the stock market had led him to wonder whether something might not happen to bring about a substantial drain on the gold supply and cause the reserve requirements specified under existing law to have to be suspended. In his opinion the existing law was clearly obsolete, having been adopted under a different set of circumstances than now prevailed. His question, therefore, was whether there should not be a re-examination of the existing law, with a view to the possibility of some change that would make it possible for the Federal Reserve System to meet any crisis without having to take emergency action.

Chairman Martin noted that this problem had been given consideration on previous occasions. The Committee might ask its staff to review the procedures involved so that everyone would be familiar with them. Some caution was indicated, because a planning exercise, if understood to be in process, could lead to comment and speculation. However, he would see no objection to putting down in a paper the facts relating to the procedures provided under the present law.

It was agreed that the next meeting of the Federal Open Market Committee would be held on Tuesday, June 19, 1962.

The meeting then adjourned.

Assistant Secretary