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, July 28, 1964, at 9:30 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Hayes, Vice Chairman
Mr. Balderston
Mr. Daane 1/
Mr. Hickman
Mr. Mills
Mr. Mitchell
Mr. Robertson
Mr. Shepardson
Mr. Shuford
Mr. Swan
Mr. Wayne

Messrs. Ellis, Bryan, and Deming, Alternate Members of the Federal Open Market Committee

Messrs. Bopp and Irons, Presidents of the Federal Reserve Banks of Philadelphia and Dallas, respectively

Mr. Young, Secretary
Mr. Sherman, Assistant Secretary
Mr. Kenyon, Assistant Secretary
Mr. Broida, Assistant Secretary
Mr. Hackley, General Counsel
Mr. Noyes, Economist
Messrs. Brill, Furth, Garvy, Grove, Holland, Jones, Koch, and Mann, 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
Messrs. Partee and Williams, Advisers, Division of Research and Statistics, Board of Governors
Mr. Axilrod, Chief, Government Finance Section, Division of Research and Statistics, Board of Governors
Miss Eaton, General Assistant, Office of the Secretary

1/ Entered meeting at point indicated in minutes.

Mr. Helmer, First Vice President of the Federal Reserve Bank of Chicago
Messrs. Eastburn, Taylor, Baughman, Parsons, Tow, and Green, Vice Presidents of the Federal Reserve Banks of Philadelphia, Atlanta, Chicago, Minneapolis, Kansas City, and Dallas, respectively
Messrs. Sternlight and Parthemos, Assistant Vice Presidents of the Federal Reserve Banks of New York and Richmond, respectively
Mr. Eisenmenger, Director of Research, Federal Reserve Bank of Boston

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the Federal Open Market Committee held on July 7, 1964, were approved.

Before this meeting there had been distributed to the members of the Committee a report from the Special Manager of the System Open Market Account on foreign exchange market conditions and on Open Market Account and Treasury operations in foreign currencies for the period July 7 through July 22, 1964, and a supplementary report covering the period July 23 through July 27, 1964. Copies of these reports have been placed in the files of the Committee.

Supplementing the written reports, Mr. Coombs said that the gold stock would remain unchanged again this week. The French had come in with their usual monthly gold order for $34 million last Friday, and $25 million would be sold to Germany on July 29. These sales had been substantially offset, however, by a purchase of $50 million from the Bank of England. The Stabilization Fund would wind up the month with a gold balance of nearly $170 million, which would be further supplemented

early in August by the United States' share, possibly as much as $25 million, of the Gold Pool receipts during July.

While the Stabilization Fund at the moment was in a fairly comfortable position, Mr. Coombs continued, there were a number of potentially heavy demands for gold which might materialize over coming months. The French demand continued to run at a rate of slightly more than $400 million a year. The Swiss National Bank was now carrying somewhat more than $200 million in excess of their traditional ceiling. The potential German demand was, of course, even greater, and Bundesbank officials had already hinted that they would like to get a substantial share of any gold which might be sold off by the British or the Dutch. The Austrians had indicated that they would like to make new arrangements for a series of monthly purchases in order to keep their gold ratio up to the 50 per cent level, and the Spaniards, who had been building up their dollar balances, might also be heard from.

On the exchanges, Mr. Coombs said, there had been some interesting developments in the guilder, lira, and sterling markets. In the case of the guilder, the Netherlands Bank had continued to pursue a tight money policy in an effort to check inflation and correct a serious balance of payments deficit. During the first five months of this year, the Netherlands ran a total balance of payments deficit of $250 million, which was a very substantial amount indeed for a country the size of the Netherlands. Largely owing to the credit squeeze, however, only

$60 million of this deficit had to be financed by drawing down the reserves of the Netherlands Bank. The remaining $190 million was financed by repatriation of short-term dollar investments by the Dutch commercial banks as their liquidity positions came under pressure. In recent weeks, repatriation of dollar investments by the Dutch commercial banks was apparently running well ahead of the balance of payments deficit, with the result that the dollar reserves of the Netherlands Bank had risen by more than $50 million and now stood close to the $200 million ceiling. To guard against still further inflows originating in borrowing abroad, the Netherlands Bank had recently prohibited the Dutch commercial banks from incurring a net debtor position in foreign exchange. If the Dutch credit squeeze continued, however, loopholes in this regulation might well appear just as had occurred in the case of France. Meanwhile, the pulling back of dollar investments by Dutch commercial banks had probably contributed to the strength of the Euro-dollar rate which remained more than one-half per cent above the 90-day certificate of deposit rate in the New York market.

Mr. Coombs reported that there had been a number of encouraging developments in the case of the lira, both political and economic. The new government seemed to be much more solidly established. The Italian credit restraint program, initiated by the Bank of Italy nearly a year ago, had brought about a decided slackening in the rate of monetary expansion. Imports were down, while exports had continued to rise.

A lot of money had come in through direct foreign investment in Italian industry, and the Italian reserves actually increased during the second quarter despite the fact that the Italian commercial banks continued to liquidate their foreign indebtedness. The New York Bank's operations in forward lira as agent of the Bank of Italy might also have contributed to an improvement in the market psychology. Rumors of a lira devaluation had subsided and the market rate on the forward lira had now declined below the 4 per cent ceiling that had been maintained. Meanwhile Italy's partners in the Common Market, some of whom had previously taken a pessimistic view of the Italian government's economic program, now seemed prepared to provide not only short-term but also medium-term financial assistance in order to cushion the transition to a solid equilibrium in the Italian payments accounts. In retrospect, the $150 million of short-term credit provided by the Federal Reserve to the Bank of Italy last winter seemed to have been a useful operation.

In the case of sterling, Mr. Coombs said, the Account Management's weekly reports to the Committee had outlined the rationale and results of the recent operations in sterling in order to forestall private arbitrage outflows to London. In general, the operations achieved their limited objectives and had provided some useful experience in a new area of operations. Both the Account and the Bank of England had been concerned over the possibility of leakages and Mr. Coombs found it gratifying that the commercial banks acting as agents succeeded in maintaining secrecy.

Finally, Mr. Coombs said, as had been anticipated the Bank of Japan had requested a renewal for a further three months of their $50 million swap drawing maturing July 30. Furthermore, the Bank of Japan expected a reserve decline of roughly $65 million in the course of this month, partly owing to measures recently taken to restrain borrowing on the Euro-dollar market, and might wish to make a further drawing in the amount of $30 million before the month's end.

Mr. Mitchell asked whether the Italian authorities had any policy with respect to foreign investments in Italian industry, and whether they felt such investments might serve to thwart their monetary policy. Mr. Coombs replied that by and large the Italian authorities had encouraged such investments. Their volume had not been great enough to thwart Italian credit policy, and some recent investments by large American corporations had helped strengthen the capital structure of certain major Italian industries. This probably had reduced the concern by the Bank of Italy that credit tightening would damage the capital structure of some Italian firms.

In response to questions by Mr. Ellis concerning the possible further swap drawing of $30 million by the Bank of Japan, Mr. Coombs said the Japanese felt that a useful purpose would be served by reducing their reserve loss in July from an expected $65 million to about $35 million. He was hopeful that the reserve loss would be temporary and soon reversed. The outlook for Japan's balance of payments had improved

since earlier this year, and the Japanese seemed determined to carry out policies to strengthen their payments situation. There was, of course, no assurance that these policies would be effective in time to permit repayment of the drawing. If the Japanese were unable to liquidate the drawing by use of current receipts, Mr. Coombs thought they probably would apply to the International Monetary Fund for a medium-term credit and repay the drawing by that means.

Mr. Mills commented that Mr. Coombs had touched on several sensitive points which seemed to him to deserve the scrutiny and analysis of academicians. The question he had in mind was how far monetary policy should be pressed to maintain the international reserve position of any individual country at the expense of undermining the economy of that country. One saw the problem in Japan where there had been a rash of bankruptcies quite recently; Japanese policy moved frequently between tightness and ease. One could see a definite slackening in the economy of Italy, and in some Latin American countries such as Argentina. In all of these countries it seemed to be reassuring that monetary measures had resulted in improving the international exchange positions. But if this was done at the expense of reducing the viability of their domestic economies, there was a question of whether the gain was worth the loss.

Mr. Coombs said he thought that a certain amount of experience bearing on this question had been built up since the war. European

countries and Japan had moved from a system of direct, selective controls more or less across the board toward greater reliance on general monetary and fiscal policies. They had not completely abandoned direct controls, but were seeking a proper blend of the two. He thought that the combination of tighter credit, fiscal measures, and certain direct controls in Europe was halting inflationary trends, so far without adverse effects on production and employment. In his judgment, these policies were working.

Thereupon, upon motion duly made and seconded, and by unanimous vote, the System Open Market transactions in foreign currencies during the period July 7 through July 27, 1964, were approved, ratified, and confirmed.

Mr. Coombs recommended that the $250 million standby swap arrangement with the German Federal Bank, which would reach the end of its three-month term on August 6, be renewed for a new and longer period of six months. He noted that the German Federal Bank would be agreeable to this arrangement.

Renewal of the swap arrangement with the German Federal Bank, with extension of term from three to six months, as recommended by Mr. Coombs, was approved.

Mr. Coombs then recommended that the $100 million standby swap arrangement with the Bank of France, which also matured on August 6, be renewed for another three-month period. It was possible that the Bank of France itself might suggest an extension of the term to six months. If so, he assumed this would be acceptable to the Committee.

Renewal of the swap arrangement with the Bank of France for a further period of three months, or for six months if the Bank of France should so request, was approved.

The possible further drawing of $30 million by the Bank of Japan on its swap arrangement with the System was noted without objection.

Before this meeting there had been distributed to the members of the Committee a report from the Manager of the System Open Market Account covering open market operations in U. S. Government securities and bankers' acceptances for the period July 7 through July 22, 1964, and a supplementary report covering the period July 23 through 27, 1964. Copies of these reports have been placed in the files of the Committee.

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

The financial markets have turned in a good performance during the past three weeks, highlighted by the Treasury's very successful advance refunding. In that operation, as you know, some $9-1/4 billion of issues maturing within three years have been exchanged for issues maturing in five, nine, and twenty-eight years. Although the turn-in considerably exceeded market estimates, the atmosphere in the market has remained quite firm and confident. Even the rumors of a possible British Bank rate increase shook loose only a few bond holdings from weaker hands and these have been readily absorbed. The dealers' stake in the refunding issues remains rather large, of course, and the market accordingly is vulnerable to news that would suggest any change in the outlook--which at present is regarded as pointing to stable rates.

A counterpart of the heavy response to the Treasury refunding has been the increased downward pressure on Treasury bill rates--which the current offering of a $1 billion strip of bills has served to ameliorate, but not

entirely to offset. Early in the past three-week period there was a substantial demand for bills on the part of sellers of eligible rights in the refunding, and by holders of the $2 billion of maturing July 15 bills. These sources of demand served to deplete dealer inventories very substantially, and since the middle of the period the more moderate continuing demand from banks, corporations, and public funds has served to maintain downward pressure on bill rates. At their low point on July 16 and 17, the 3-month bill was bid at 3.42 per cent, compared with 3.50 per cent at the start of the recent period. Rates moved up only briefly and moderately after the Treasury's bill strip was announced, and yesterday the 3-month bills were sold at an average rate of about 3.48 per cent. It may be that payment for the strip of $1 billion Treasury bills tomorrow, followed by the sale of $1 billion of 1-year bills on Thursday, and by the sale of another short-term security to refund the remaining August 15 maturities, will serve to put some supply back into the short-term area and tend to bolster short rates, but on the other side it is to be expected that investor demands will continue and the System will also have to be a sizable buyer of short issues in meeting forthcoming reserve needs. Once the books on the Treasury's August 15 refunding are closed we may be able to effect some part of that provision of reserves through purchases of coupon issues, without buying in an area too close to the Treasury's offering, but in any event the prospective reserve need seems too large to be met without further sizable purchases in the short-term area.

System operations were substantial during the past three weeks, as the Desk sought to preserve a steady market background during the Treasury's refunding operation. Reserves were injected over the first several days, then withdrawn in large volume against the background of an easier money market, and then in the past three days re-injected in anticipation of reserve drains through the impact of market factors. Federal funds traded mainly at 3-1/2 per cent, but in larger volume than had prevailed in recent months, and there was trading below 3-1/2 per cent on several days, especially toward the end of the July 22 week.

The Treasury will be announcing tomorrow its plans for refunding the remaining $4.1 billion of August 15 maturities, of which some $2.2 billion are held by the public. Given the modest size of the maturities and the solid condition of the market, this job should be quite routine. Indeed, the major question for the Treasury would seem to be how this operation might be adapted to deal most effectively with the problem of

the short rate. The current expectation is that the Treasury will offer a short note, but some further offering of bills is also a possibility.

Thereupon, upon motion duly made and seconded, and by unanimous vote, the open market transactions in Government securities and bankers' acceptances during the period July 7 through July 27, 1964, were approved, ratified, and confirmed.

Chairman Martin then called for the staff economic and financial reports, supplementing the written reports that had been distributed prior to the meeting, copies of which have been placed in the files of the Committee.

Mr. Koch presented a statement on economic conditions as follows:

Recently released second quarter GNP figures show that economic expansion thus far in 1964 has been about on target as projected early in the year by the Council of Economic Advisers. Moreover, many of the more comprehensive indicators of economic activity continue to rise and seem gradually to be reflecting the effects of the tax cut. Industrial production in June, for example, was one-half per cent above May and 4 per cent above the end-of-1963 level. Retail sales in July are apparently advancing further from the record May- June level.

Yet the "too-good-to-be-true" picture of the economy seems to be losing a bit of its luster. This current impression may reflect merely the onset of the usual summer doldrums or even an economist's penchant for feeling better when he can find something wrong. Nevertheless, some economic indicators have not done so well recently. The rate of unemployment rose again in June and no doubt continued high in July, while the rate of expansion in employment has been tapering off. Although housing starts were up a little in June, they have been drifting downward on balance since last fall. New orders received by all producers of durable goods declined slightly again in June, although those of machine tool builders rose sharply.

Some uneasiness about the future course of the economy stems also from the structure of the expansion during the first half of the year. Early in the year the likelihood of as much

expansion as projected was questioned if so much of it had to depend on increased consumer spending on nondurable goods and services. Yet it is just this category of spending that has increased so sharply over the past six months. The January projection called for an increase in consumer spending on nondurable goods and services during the first half of about $12-1/2 billion, or almost 4 per cent. The estimated actual increase turned out to be only a little under this projection. Although we can expect some drop in the personal saving rate from its current level, temporarily at about 8-1/4 per cent as a result of the tax cut, one wonders whether consumers can continue over the next six months and longer to increase their spending on nondurable goods and services as rapidly as in the recent past.

Consumer spending on durable goods has risen much less sharply this year, particularly recently. Dealer deliveries of new autos have declined moderately since mid-June, but shipments from assembly plants in the East were limited by a trucking strike that ended last week. I have already noted the slowing down in housing starts.

In the business sector, the main news is in the inventory area where stocks continue moderate in view of the further rise in sales. The rise in inventories in recent months has been in goods-in-process and finished goods rather than in raw materials and purchased stocks. In other words, businesses are expanding their inventories where needed to meet customer demands for quick deliveries. But with supplies of materials still generally ample, with delivery times still showing few signs of lengthening, and with industrial wholesale prices remaining relatively stable, businesses are not rushing to stock up in anticipation of future needs.

In the important wage-price-profit area, it is still too early to predict the likely outcome of the current bargaining activity in the auto industry. The recent labor-management agreements in the rubber and oil industries involved fringe benefits, whose total costs are very difficult to estimate, but there were no wage increases. These settlements do not appear to have been out of line with either cost stabilization objectives or settlements reached in other major industries earlier in the year. In manufacturing as a whole, unit labor costs, including fringe benefits, are down from early in the year, with the first half rise in money earnings being the smallest since the recession year 1954.

Recent price changes have been mainly in markets for foodstuffs, and largely reflect seasonal influences. The wholesale industrial price index has remained stable. Most

prices are not changing. The evidence suggests mainly selective bottleneck-type upward pressures, such as in the case of some nonferrous metals.

With prices remaining relatively stable and unit labor costs, at least in manufacturing, down a little, profit margins are up further. Higher business sales and profits have led to some upscaling of capital investment, but thus far such investment can hardly be called ebullient. It is clear that businessmen are reluctant to overbuild capacity.

Difficult as it always is to foresee sources of future economic strength, it is in the business fixed capital spending area, in State and local government spending, and in the area of consumer spending on nondurable goods and services that we must probably seek the sources of further aggregate expansion.

Since State and local spending and consumer spending on nondurables normally rise gradually and since the further rise in business fixed capital spending is now projected by businessmen at a rate that is within reasonable bounds, most projections of over-all economic activity this year call for continued moderate expansion.

And with the unemployment rate remaining high, this further moderate expansion in over-all economic activity again raises doubts as to the likelihood of bringing the rate down significantly in the foreseeable future. Indeed, with the unemployment rate of nonwhite teenagers over 30 per cent, one basic cause of our recent race riots becomes painfully clear. As for capital utilization rates, that for major materials production has been unchanged since April and that for manufacturing is up only moderately from a year ago. Current rates are unlikely soon either to limit the rise in physical production or to induce widespread price boosts.

Thus, in conclusion, domestic economic developments as a whole still seem to me to call for expansionary Government economic measures, including a stimulative monetary policy.

Mr. Brill made the following statement concerning financial developments:

After several months of rather placid existence, financial markets were stirred into some turbulence over the past three weeks, principally by debt management operations and an assist from rumors of a British Bank rate increase. The turbulence was mild considering the magnitude of the debt management operations. The Treasury advance refunding, involving $27

billion of publicly-held debt, resulted in a removal of $4-1/2 billion of short-dated instruments from the market and almost $5 billion of shorter intermediates. To fill the gap created at the short end, which was causing downward pressure on short-term rates at a time when rates abroad were rising, the System and the Treasury sold bills, the Treasury rushed out a $1 billion bill strip, and it indicated that forthcoming offerings would also be in the short area.

As the dust settles, we find long- and intermediate-term rates on Government securities only a shade higher than early in July and short-term rates a bit lower, a remarkably small price reaction in light of all the fund flows involved. The dust hasn't completely settled, for dealers still have substantial positions in the new issues, with more Treasury financing imminent, but they do not appear unwilling to carry substantial inventories of coupon issues in light of current market attitudes and expectations.

The market's ability to absorb such a lengthening in maturity in the Federal debt with minimal price adjustment is the latest indication of the tremendous savings volume the private economy continues to generate. Financial saving by the private sector has continued high this year, as it has throughout the recovery and expansion period, and recently it has been given an extra boost by the tax cut. What is different this year, however, is not so much the volume of saving as its compositon. Two differences in savings patterns have emerged in 1964, neither, unfortunately, readily susceptible to explanation.

First is the shift in composition as between financial intermediaries and direct market investment. From 1961 to 1963 the bulk of private financial savings flows--well over four-fifths of the total--went into financial intermediaries. This contrasts with 1959, the previous high saving year, when only one-half went to intermediaries and the other half, responding to rising market rates, went into direct purchases of securities. So far in 1964, savings flows have tended to revert to the 1959 pattern, with the flow to institutions lower and the flow into securities increasing sharply.

What is surprising about this shift is that it has taken place without the usual change in interest rate relationships. One of the few stable functional relationships we have been able to discern in financial flows is that when there was a widening of the spread between market interest rates and the rates offered by institutions, the share of private savings

flows directed into market instruments increased, and when institutional rates began to catch up with the market, a larger share of the savings flow was diverted through financial intermediaries. It is comforting to econometricians to have an economic relationship that makes common sense and also yields a high "r^2," and it is disconcerting when such a previously firm relationship fails to work. It isn't working now. The pattern of flows so far this year would be more consistent with a substantially higher level of market rates than has actually prevailed, given the level of rates offered by banks and savings associations.

There doesn't seem to be any easy explanation of this deviation. Perhaps savers have reached some saturation point in their ownership of savings accounts and want to diversify their portfolios regardless of current rate relationships. Perhaps confidence in the future stability of prices is permitting savers to waive any inflation risk premium when acquiring long-term debt instruments. There are many possible explanations, but none that can now be supported empirically.

Another puzzling development in savings flows is the recent rise in the public's demand for cash balances. The money supply rose substantially in June, even while Government balances were increasing, and has continued to increase thus far in July when Government deposits are being drawn down. Based on required reserve figures through July 22, it seems likely that the money supply will show an annual rate of expansion of over 8 per cent in both June and July, after rising at only a 2 per cent rate over the first five months of the year. It is hard to find in the available evidence any explanation of this sudden surge in cash balances, particularly since in the current state of financial statistics we don't even know who is holding the larger balances, let alone for what purposes. There is nothing in surveys of consumer or business spending intentions to suggest that the private sectors are girding themselves for a spending spree. One hypothesis is that the rise reflects a sort of inadvertent accumulation of tax saving, being held idle until consumers and businesses decide how to commit the funds. This has some elements of plausibility, but again is unverifiable.

Before attempting to read too much significance into a two-month development, however, it should be recalled that growth in the money supply is not always smooth. For example, there was a spurt in the money supply last November of about the same order of magnitude as that which occurred this June, but it didn't seem to result in any significant change in the

course of the economy, financial or otherwise. It may be that the recent surge will soon spend itself.

This is not to belittle expansion in the money supply at an 8 per cent annual rate, or to cast doubt on the validity of the figures. It is just that recent increases do not seem to have significant corollaries in any other economic development of which we are aware. In the context of an economy that shows no signs of overheating, that seems to have reached a plateau in its use of plant and labor resources, and that still generates a large volume of long-term saving, a rapid increase in the money supply for brief periods is cause for inquiry and study, but not necessarily for alarm.

Mr. Furth presented the following statement on the balance of payments:

The payments deficit for the second quarter turned out somewhat smaller than expected three weeks ago but the tentative figures for the first three weeks of July were disappointing.

The deficit was $140 million in June, and $675 million in the second quarter, after adjustment for seasonal influences and "special" transactions.

For the fiscal year 1964 as a whole, the deficit amounted to $1.8 billion--still too large a figure but by far the lowest twelve-month total in seven years. And it is particularly gratifying that it could be financed in such a way as to keep the decline in U.S. reserves and the increase in liabilities to foreign monetary authorities to a minimum. More than two-thirds of the total was covered by "special" receipts and by the increase in dollar holdings of foreign holders other than monetary authorities. Nearly all the rest was financed by medium-term credits, including the issue of Roosa-bonds and drawings on the International Monetary Fund. U.S. gold holdings declined by only $200 million, while U.S. holdings of foreign convertible currencies actually rose and liquid dollar liabilities to foreign monetary authorities declined.

Moreover, the deficit was nearly equalled by a rise in U.S. liquid claims on foreigners. Bank-reported short-term claims alone increased by $1.3 billion, and long-term bank loans by an additional $0.7 billion.

Notwithstanding the comfort we may derive from the results of the past twelve months, the July figures are disquieting. The tentative data for the first three weeks of the month indicate a deficit of $560 million. July always shows a sharp seasonal deterioration in the U.S. payments balance, but this year's increase in the deficit over and above June seems to be far larger than seasonal.

Unfortunately, we do not know the causes of that increase. It is true that sharp increases have been observed during the first month of every recent quarter: January 1964 was much worse than December 1963, April much worse than March; and the second and third months of each quarter have always shown considerable improvement. But the trend is disturbing: April was worse than January, and July seems likely to be worse than April.

The prospects of improving the payments balance in the short run by monetary policy depend, of course, on the reasons for the deterioration. Insofar as a decline in foreign demand for our exports, or an increase in our Government expenditures abroad, was responsible, monetary policy could do little about it. Insofar as an increase in our imports or in our expenditures for foreign travel was a factor, monetary policy--apart, of course, from its perennial role as guardian of price stability--could correct the situation only by action severe enough to temper the rise in our national income.

On the other hand, insofar as we were to find a sudden increase in the outflow of money-market funds into foreign-currency assets, relatively small changes in covered interest rate differentials might be helpful. But during the second quarter these flows were, on balance, quite insignificant, and we have no indications of any substantial increase in recent weeks. Flows into the Euro-dollar market were indeed large in recent months and may have risen further. But the impact of these flows on the U.S. payments balance may not be easily affected by U.S. monetary policy: any measure designed to curtail them may, after a brief lag, not only raise interest rates in the Euro-dollar market but perhaps also divert borrowers from that market to U.S. banks.

Finally, we might find that there was an unusually rapid increase in direct investments abroad and in U.S. bank credit to foreigners. We have no data on direct investments for the second quarter, and no complete data on bank credit for any month after May. But we know that all types of bank-reported claims on foreigners together rose in June by the unusually

large amount of $340 million; and if I had to make a guess, I should say that bank credit and direct investments could well have contributed significantly to the recent deterioration.

If the U.S. payments deficit were to continue at the level of the past three weeks, and if a rise in U.S. investments and credits were indeed found to be playing a large role, U.S. monetary policy would be faced with the question of how best to deal with the problem. At the moment, however, we lack the information needed for an appropriate answer.

Chairman Martin then called for the usual go-around of comments and views on economic conditions and monetary policy, beginning with Mr. Hayes, who presented the following statement:

The most significant aspect of the last three weeks' developments has been the reappearance of a very serious balance of payments deficit--at least on the basis of partial data available so far for July, together with data indicating that the June deficit was more serious than it had seemed to be at first glance. At the same time, the latest domestic statistical data point to a continuing favorable business situation and a prospect of further expansion. However, there are presently no signs of any acceleration, and there were even indications of leveling off in some sectors in May and June--although these signs were slighter in June than in the preceding month.

Plant and equipment spending seems likely to continue its upward course; and the absence of inventory build-up in the first half of 1964 may point to an increase in stimulus to production from this source in the second half. Consumer spending is a major element of strength in the economy. The May rise in retail sales now appears to be stronger than reported earlier, and the advance report for June indicates maintenance of the high May level, with further advances in early July.

Prices continue to exhibit remarkable stability--but the cost-price outlook is still clouded by the unsettled automobile pay negotiations.

Recent balance of payments figures give cause for considerable concern. Preliminary data for the first three weeks of July show an aggregate over-all deficit of about $550 million. We have no way of analyzing what lies behind this huge deficit.

It may reflect errors that will lead to drastic revision--but it is so large that even after a sizable revision we would still face a very disturbing problem. Paradoxically enough, the press has recently been filled with optimistic appraisals of the balance of payments outlook, based largely on the relatively low annual rate of deficit of about $1.6 billion in the first half. This optimistic point of view ignores two important facts: (1) that even a deficit of this magnitude presents serious financing problems in this seventh year of major deficits; and (2) that the trend within the first half was adverse. The latter point gains greater weight in the light of what seems to be happening in July.

The modest June deficit should be assessed against the background of a sizable reflux of corporate time deposits from Canada during that month, which caused Canadian balances in this country to fall by $200 million. In the absence of the sharp decline in our liabilities to Canadian banks, the deficit would have been in the $300-$400 million range. Another ominous development is a very substantial upsurge in June in bank-reported claims on foreigners, estimated tentatively at over $300 million and apparently reflecting very large short-term bank loans. The fact that the trade surplus seems to be holding up at a relatively high level, together with the increasingly tight credit conditions abroad and the evidence of deterioration in our short-term capital account, suggests that monetary policy might well be looked to as at least a partial remedy of our payments problems.

More complete banking data now available for June confirm the picture of moderate strength already evident three weeks ago. Money supply, money supply plus time deposits, and bank credit rose more rapidly than their average monthly increases earlier in 1964. If we include preliminary figures for the first half of July, the money supply has grown at an annual rate of 4.3 per cent so far this year, exceeding the 3.8 per cent of a year earlier. For money supply plus time deposits this year's gain still lags somewhat behind last year. But it is striking that despite the sizable business expansion and despite a number of minor policy changes toward less ease on the part of the Committee, there is no solid evidence of a slow-down in credit growth, and we have continued to provide liquidity to the economy on a very generous scale. I am pointing to this not critically but to emphasize the point that a switch to a slightly less generous credit policy would probably involve only minimal risks to domestic business.

We may all find great satisfaction in the debt extension achieved in the Treasury's highly successful advance refunding program. The program did, however, put heavy downward pressure on short-term interest rates--pressure which fortunately has been partly offset by the Treasury's offering of a strip of bills and a one-year bill, and the prospect of a short-term obligation to replace the remaining August 15 maturities. Nevertheless, demand for short-term securities, including System purchases to offset seasonal pressures on bank reserves, will remain heavy for the next couple of weeks.

A change of policy at this time is precluded by the necessity of maintaining stable money market conditions to facilitate the August 15 refunding and to permit the market to digest the huge advance refunding just completed. I would hope, however, that within the existing policy the Desk would do what it could to maintain as firm a short-term rate structure as possible, in view of the pull being exerted on American funds by foreign rates. The existing directive might well be renewed with only minor changes to reflect the altered Treasury financing outlook and the accelerated deterioration in the balance of payments in July.

Looking a little further ahead, I am impressed anew by the lack of progress in coping with our very serious balance of payments problem and the necessity of giving adequate emphasis this problem in the formulation of monetary policy. To me is unthinkable that anyone should contemplate abdicating our responsibilities for maintaining the international strength f the dollar and relying on the vague hope that some other ranch of Government, using more "specific" measures, will take is burden from our shoulders. In other words, I think it ghly probable that within the next month or two, in the sence of an unexpected improvement in the balance of payments, we shall have to take some moderate but clear-cut action in the direction of less credit ease.

Unfortunately, public opinion is none too well prepared for such a move, in view of the many optimistic statements on the dollar's status in recent months. Probably a loss of gold is the most convincing sign of international financial trouble to the general public, and of course for a variety of reasons the loss has been nil for many months. Moreover, it is even possible that a sterling crisis could bring some temporary additions to the gold stock and thus render more difficult this psychological obstacle to acceptance of a more restrictive policy. Under these conditions I feel that it is up to the System to try to prepare the ground, both within and outside of

> the Government, for whatever action seems likely to be called for fairly soon if the international danger signals now clearly flying are confirmed by actual payments developments in the coming weeks.

Mr. Ellis commented that in New England consumer spending seemed to be strengthening, according to recent data on department store sales and new car registrations. Business capital spending continued to rise, and nonresidential building contract awards were running 12 per cent above a year ago. In a recent survey of the one hundred largest manufacturing corporations in the District, second-quarter sales were reported to have substantially exceeded expectations, and more than two-thirds of the firms expected third-quarter sales to be at least near the second-quarter levels.

Insured unemployment claims in New England were 12 per cent below last year, and new lows were expected later this year. Nonagricultural employment was up, although manufacturing employment had yet to regain its earlier level. Manufacturing output, on the other hand, continued to rise slowly. Shoe production in May was less than last year, and for the first five months of 1964 was about 1 per cent below the level last year.

Financial activity continued to outpace production, Mr. Ellis remarked. Business loan expansion around the tax date in June was sharper in the District than in the nation. However, demand deposits continued to show almost no growth, and today were at about their 1962 level. The scramble for deposits continued to be intense. Since

January the volume of CDs outstanding in New England had expanded 34 per cent, in comparison with 24 per cent for the United States as a whole. In New England the loan-deposit ratio had reached a new peak of 71 per cent, and at Boston banks the ratio was 75 per cent, compared with 66 per cent for all member banks.

Turning to policy, Mr. Ellis said it seemed to him that there were three aspects of the current economic situation to be taken into consideration. First and foremost, there was the continued balanced expansion of the economy without excesses. The expansion was so nearly ideal that the burden of proof seemed to rest on anyone who wanted to alter conditions. This led to the second major aspect, the pattern of credit expansion. In June total reserves had risen sharply--at a seasonally adjusted annual rate of over 16 per cent. As had been pointed out, the recent record suggested that a one-month bulge in reserves tended to be followed by slower growth rates in subsequent months. But it appeared obvious that if such a rate of expansion continued it would call for attention.

The third element to be taken into consideration, Mr. Ellis said, was the recent worsening in the U. S. balance of payments position. The outlook seemed to be for a resumption of outflow of short-term balances, as a result of widening covered yield spreads.

Given the present situation, Mr. Ellis' choice of policy would be to seek net free reserves between zero and $100 million, and to

support the Treasury bill rate as necessary, gradually moving it into the 3.50-3.60 per cent range as a small precaution against the effects of higher short-term rates abroad. This policy would be in the context of letting the dust settle after the recent advance refunding. He would hold a discount rate increase in abeyance. Like Mr. Hayes, he was concerned that the public be prepared before any significant move toward less ease was undertaken.

Mr. Irons reported that economic conditions in the Eleventh District had changed little during the past few weeks. There had been a moderate upward movement in June and in the first part of July. Industrial production was running about 5 per cent above a year ago and was inching up. Production had been held down a bit by a decline in crude oil output, and it was likely that crude oil allowables would be reduced slightly in August. Construction was very strong, and the outlook, especially for residential construction, was favorable. Employment had moved about seasonally and the unemployment rate, not seasonally adjusted, was about 4-1/2 per cent of the labor force. This was somewhat below the year-ago figure of 5 per cent. Retail trade, including auto sales, was very strong.

It was too early to say much about agricultural prospects for this year, Mr. Irons continued, but there had been an increase in acreage and crops generally were satisfactory. The situation was about normal for this season. Cash farm receipts for the year to date were running between 5 and 6 per cent below a year ago.

On the financial side, Mr. Irons said, loans at District banks had increased, while investments and deposits were down slightly. There were no large changes one way or the other among loan categories, but commercial and industrial loans were down and loans in other categories were up. Demand for Federal funds in the District had been strong. Borrowings at the Reserve Bank were higher, but the change was not great; a few more banks, both small and large, were coming in to the discount window.

In the light of the domestic and international situation, and of the Treasury financing situation, it seemed to Mr. Irons that there was no reason at the moment to make any strong policy change. The domestic economy was undergoing steady expansion with a good degree of price stability, and there was a lack of evidence of any imbalances. There had been some deterioration in the balance of payments situation in recent weeks, but in his judgment an overt policy change was not called for as yet by either domestic conditions or foreign developments. He would like to see continued moderate expansion in bank credit, relative stability on average in the money market, and levels of interest rates and a degree of reserve availability approaching those of the last three weeks. His guidelines would be free reserve averages of $100 million, plus or minus about $25 million; a Treasury bill rate around 3.50 per cent, plus or minus about 5 basis points; and the Federal funds rate also at 3.50 per cent. He would not raise the discount

rate at this time. The draft directive with the minor changes proposed by the staff was acceptable to him. He would prefer that any errors on the part of the Desk be on the side of a little more firmness rather than a little more ease.

Mr. Swan reported that, as in the Eleventh District, there had been no very significant changes in the immediate situation in the Twelfth District. The rate of unemployment in the Pacific Coast States was unchanged in June, which was a little unusual in contrast with the increase in unemployment in the nation. However, the District unemployment rate still continued well above that of the country as a whole and in May and June was little changed from June of last year. The failure of unemployment to worsen was related to the fact that the decline in employment in defense-related industries in June was the smallest monthly drop so far in 1964. The rate of these decreases had been lessening, but some further declines in defense employment were anticipated.

Lumber prices, while still below year-ago levels, were somewhat firmer in July, Mr. Swan said. The firming occurred against a background of a steady flow of orders and some vacation shut-downs.

Cash farm receipts for the first five months of the year in the District were slightly higher than a year ago, but had shown less increase than in the nation as a whole. Agricultural production prospects seemed to be better; crop volume in the District was likely to be heavier in 1964 than in 1963. Department store sales in the first part of July

continued at levels well above a year ago. On the whole, the economic situation in the District appeared quite favorable.

Twelfth District banks reflected some pressure in their reserve positions, Mr. Swan noted. The larger banks were net buyers of Federal funds in the week ending July 8. They moved to the selling side in the next two weeks, but in relatively small amounts.

Mr. Swan reported that one of the smaller city banks recently had borrowed from the Reserve Bank to tide over until it could sell some mortgages. Its borrowing need had been occasioned by the fact that a rather substantial certificate of deposit, held by a savings and loan association, had not been renewed as expected, and the bank felt its only recourse was to sell mortgages. Mr. Swan said he did not know whether or not this would prove to be the first of a number of such incidents, but he suspected that it might be.

It seemed to Mr. Swan that with an advance refunding just accomplished, and with additional Treasury financing ahead, the Committee should maintain an even keel situation in the next three weeks. In his judgment the domestic situation did not call for a policy change in any case. Recent developments in the balance of payments certainly were not encouraging, but given the lack of knowledge thus far as to the cause for the deterioration, and given the fact that the figures were tentative and had been subject to substantial revisions in the past, he saw no basis as yet in the international situation for a change in policy.

Thus, Mr. Swan favored a continuation of the Committee's policy of the past three weeks, without any attempt to obtain slightly more firmness within the framework of current policy. He was satisfied with the draft directive that had been prepared by the staff, and would not change the discount rate.

Mr. Deming reported that Ninth District economic activity expanded in June, apparently more than seasonally, and the expansion seemed to have carried over into July. Total industrial power use in June was up 12 per cent. While total employment, seasonally adjusted, had shown little change from January to July, manufacturing employment in Minnesota moved up in July from June levels. By the close of June, iron ore shipments from Lake Superior ports were 23 per cent ahead of the same period last year. Nonresidential construction activity was moving ahead steadily, although residential building was slowing down.

June bank debits, seasonally adjusted, for the Ninth District showed the sharpest month-to-month rise this year and were 18 per cent ahead of last June, Mr. Deming said. June personal income, however, probably would show some decline from May, in large part due to the new wheat program which caused cash sales receipts of farmers to drop, although much of this drop would be made up with certificate payments later. Agricultural output in the District in 1964 should be favorable, as growing conditions were good. Total wheat production should exceed last year's level by 10 per cent due to higher yields. Feed grain

production was estimated on July 1 as slightly smaller than last year. A strike at the Duluth-Superior docks by grain handlers had embargoed grain shipments to those ports since July 6 and had caused grain to back up to local farm storage.

District retail sales in July seemed to have improved over June, Mr. Deming continued. Department store sales were quite strong in the first half of the month in the city areas and even in the smaller urban centers where they had been weak so far this year.

The Minneapolis Bank's regular opinion survey on short-term prospects, taken as of July 22, indicated general optimism. Only two respondents foresaw some weakness in the next several weeks; about two-thirds foresaw improvement, and about one-third stability at present high levels.

Bank credit expansion had moderated somewhat so far in July, Mr. Deming said, as investments declined slightly more than loans grew. At city banks, however, loan demand in July was stronger than usual with the increase in business loans rather marked. So far this year, business loan demand at city banks had been weak, in large part apparently reflecting lessened demand for credit by grain processors who were reducing inventory as a result of the new wheat program. Some rebuilding of inventory was now taking place, but the amount of credit required by the milling trade probably would remain smaller than usual since the new program resulted in lower cash prices, and certificates did not have

to be purchased until or after actual grain processing. The net result was that the Government would, in effect, carry about one-third of the inventory cost.

With respect to policy, Mr. Deming said, it seemed to him that for the next three weeks the Committee had to stay about where it was at present; the Treasury financing situation was the dominant consideration. There also was no particular reason to change policy on grounds of the domestic economic situation. However, he had begun to share the concern expressed by Mr. Hayes and others about the deterioration in the balance of payments. In his judgment the Committee would be well advised not only to keep this problem in mind but also to look toward monetary policy action that hopefully would moderate such outflows of short-term funds that might be taking place. The Minneapolis Reserve Bank recently had learned of some cases in the District in which corporations with very strong cash positions were moving funds to Canada. Other corporations were inquiring into the possibilities of doing the same. Mr. Deming commented that it would be hard to say how much of a change in rate differentials would be required to stop such flows.

Mr. Deming concluded by saying the staff draft of the directive was acceptable to him. He would not change the discount rate.

Mr. Helmer reported that business trends in the Seventh District continued to develop favorably and, allowing for seasonal trends,

employment appeared to be increasing and unemployment to be decreasing slightly.

A local steel producer reported that auto firms were ordering steel as though they expected to continue output without a work stoppage. Current estimates for the auto industry placed output at 1-1/2 million units in the third quarter--12 per cent above last year--with about 900,000 of these being 1965 models. Order backlogs had been rising for some types of steel (mainly plates and structurals) and for some types of capital equipment (especially machine tools and heavy presses), but there was little evidence that District business firms were paying or obtaining higher prices for goods.

Business loans declined at District banks during the past few weeks, although by an amount less than usual for July, Mr. Helmer noted. Trade and metals manufacturing firms had reduced borrowings rather sharply but these reductions had been offset in part by net increases in most other industry groups, especially public utilities. The continued rise in "other" loans suggested that consumers might have stepped up the pace of their borrowing. Although most District banks had maintained fairly comfortable reserve positions, borrowing at the discount window rose temporarily in the week of the Treasury's refunding. Banks in Chicago apparently had no difficulty acquiring desired amounts of CDs, and the amount outstanding had been restored to the pre-tax date level.

Mr. Tow said there was little evidence of accelerating economic activity in the Tenth District.

Nonfarm employment had declined slightly this year. In a majority of States, employment had been essentially unchanged, but a decline in three States had produced an over-all District decrease. Most important had been a halt in Colorado's long postwar expansion, along with employment declines in Kansas and Oklahoma as contributing factors.

Farm income prospects in the Tenth District for the last half of this year were distinctly better than the first half, when cash receipts from farm marketings decreased 6 per cent. With wheat production a fifth higher than last year's relatively small crop, cash receipts from that source should materially improve. While wheat prices were lower than last year, this effect should be more than offset by an increased volume of marketings and certificate payments under the new Federal wheat program. Receipts from cattle sales also should improve, as a larger volume of marketings should at least offset the effect of lower cattle prices. Cattle prices strengthened somewhat in June and since then had remained above their May lows.

Asset growth of Tenth District weekly reporting banks this year had about paralleled that of a year ago, Mr. Tow noted. A more rapid rate of loan growth had been accompanied by a marked increase in liquidation of investments. Business loans, however, had decreased,

in marked contrast to a large expansion last year. In fact, loans to durable goods manufacturers constituted the only broad category of business loan expansion. The faster growth in total loan volume this year stemmed largely from expansion in loans to nonbank financial institutions; banks, brokers, and dealers; and real estate loans. The composition of the more rapid total loan volume expansion in Tenth District weekly reporting banks over a year ago raised real doubt as to whether it was related to growth in economic activity within the District.

Mr. Wayne commented that business activity in the Fifth District continued to rise at a slow, steady pace, following a trend that had been in progress for many months. The Bank's latest survey showed businessmen viewing the near future with about the same degree of optimism as was indicated three weeks earlier. Manufacturers on balance again reported small gains in new orders and shipments and a slight upward tendency in employment, wages, and the outlook for profits. The textile business seemed stronger and more stable than at any time in the past several years. New orders continued at a good pace, keeping backlogs large and prices firm, and profits were expected to be the best in more than a decade. Building activity remained at record levels, but stability in seasonally adjusted construction employment since early in the year and spring declines in both contract awards and building permits might foretell a leveling off sometime in the near future.

Retail sales apparently continued at generally high levels. In agriculture, July rains had brightened crop prospects quite generally.

The rather fragmentary information that had become available since the Committee's last meeting suggested that the U. S. economy was continuing to move ahead at a moderate pace, Mr. Wayne continued. It was true, as Mr. Hayes had suggested, that there were a number of question marks; the leading indicators had been showing some weakness for two months, contract awards and housing starts had been trending downward, and durable goods sales did not look particularly strong. But it seemed significant to Mr. Wayne that the advance was proceeding at a good pace in the face of such factors without any signs of inventory excesses.

Mr. Wayne believed that recent rates of expansion in reserves and bank credit had been generally appropriate to domestic business conditions. Disparities between domestic and foreign money rates continued to occasion concern and should significant short-term outflows be stimulated, reconsideration of the posture of policy might be in order. For the present, however, Mr. Wayne saw no reason either in the domestic or the international situation for altering the Committee's position. Accordingly, and also in view of the Treasury financing, he favored no change in policy and would leave the discount rate at the present level. Mr. Wayne indicated that he was satisfied with the draft directive prepared by the staff.

Mr. Mills said that, assuming that the reported financial statistics faithfully reflected the performance of the national economy and international movements of funds, in his judgment no change in policy was called for at this time. However, he continued to be disturbed by the Committee's concentration in policy actions on maintaining a predetermined level of interest rates. In his belief, the result was to draw a curtain over what otherwise would be a visible and desirable interplay of financial market factors that would offer the Committee advance notice of impending developments on which policy actions could be formulated. The Committee was now precluded from formulating policy in this way by the lack of availability of signs.

Mr. Robertson said that he shared some of Mr. Mills' concern. He then made the following statement:

> Given the reported steady expansion in business activity, the stability in the price picture, and the persisting high level of unemployment, it seems to me that a "steady in the boat" posture for monetary policy continues to be very much in order.
>
> I am not indifferent to the unfavorable recent balance of payments developments, but I continue to feel that the credit flows contributing most to the recent changes are better dealt with by a selective approach to the few lenders involved rather than by general monetary measures. On the domestic side, money supply increases have been substantial in June and July, but as yet I see no cause for concern in that development. A significant part of the July increase reflected transfers of deposits from Government to private hands, rather than a continuation of the strong net bank credit and deposit creation recorded in June. Two such months do not make a trend. Moreover, within the money supply total the recent cessation of growth in currency in circulation should lead us to accommodate a little stronger rate of growth in the demand deposit component of money.

> Finally, these money supply increases ought to be viewed against the perspective of the very appreciable shrinkage in the public's holdings of other liquid assets that resulted from the Treasury's advance refunding. With all these counteracting influences operating on over-all public liquidity, I am glad that monetary policy has been as expansive as it has.
>
> Even apart from all these other considerations, however, I think the Committee ought to feel impelled to follow an "even keel" policy over the next three weeks because of the status of the past and prospective Treasury financings. Dealers still hold a very large amount of the longer-term advance refunding issues, and now the Treasury will be announcing a separate refunding offering for the August 15 maturities (presumably a reasonably short-term offering for which the books would be open some time next week). The latter should be a routine operation, on which the Treasury, from its point of view, would not need any help. Nonetheless, we must remember that we have ordinarily maintained an "even keel" policy during and at least for a few days after the subscription periods for coupon issue refundings, and that the market has come to expect this from us as a regular practice
>
> I favor a clear-cut understanding of the "rules of the game" between us and the market, and therefore I would not want to see us break this one by a departure from "even keel" unless the need therefor is substantial. I see no substantial need to break this rule, and therefore I advocate a policy of "no change" between now and the next meeting of the Committee.

Mr. Robertson added that in his opinion the directive with the amendments proposed by the staff was clearly appropriate. He would hope that no attempt would be made to slip sideways into a tighter position, as some had suggested.

Mr. Shepardson said that while the general outlook was encouraging it seemed to him that many of the public statements being made about prospects for the domestic economy were perhaps too optimistic and that the uncertain foreign situation provided some cause for concern.

However, with the present Treasury financing activities calling for maintaining a stable situation, it seemed inappropriate to make any change in policy. Accordingly, he favored a continuation of the policy of the last three weeks. Unlike Mr. Robertson, Mr. Shepardson was inclined to feel that within the constraints imposed by the Treasury financing the Committee should not avoid moves in the direction of a little lower free reserves, and a little higher levels of short-term rates, somewhat along the lines Mr. Ellis had suggested. Mr. Shepardson approved of the directive as drafted by the staff.

Mr. Mitchell commented that he thought monetary policy should be accommodative of the needs of the economy, which he would define under present circumstances as continuing what it had been doing. He was puzzled by the behavior of the money supply during recent weeks, as was Mr. Brill, and he was uncertain of the significance of recent balance of payments figures, as was Mr. Furth. But until some further knowledge was available on the implications of these developments he would be inclined to continue policy as at present. Treasury financing also precluded a policy change. The draft directive submitted by the staff was agreeable to him.

Mr. Mitchell said he would like to comment on Mr. Hayes' suggestion that the Committee should be preparing the public for something. He was not sure what it was the public should be prepared for, but he had a feeling that it was a recession. His reason for

saying this was that it seemed pretty clear by now that the tax cut had not had the stimulative effect that had been sought. It was possible that there would be a delayed reaction, but in his judgment the goals sought had not been realized. He was not sure of the reason; perhaps the effects of the tax cut had been counteracted by the trend of Government expenditures. In any case, Mr. Mitchell thought that the Committee might well face a situation this fall in which some expansive contribution would be expected from monetary policy on domestic economic grounds. He fully shared Mr. Hayes' concern about the balance of payments, but he did not think that the sort of remedy Mr. Hayes proposed was one that the Committee was free to use. Not only was the domestic economy the Committee's greatest concern, but the strength of the U.S. economy was of the greatest importance throughout the world.

It seemed to Mr. Mitchell that monetary policy in recent years had been outstandingly successful in accommodating the economy. He thought the Committee should be very careful in making any departures in its policy on the grounds that the balance of payments situation required them, particularly since it appeared that the end of the current cycle might well be near. In his judgment it was most important that the System avoid the collison course on which it would embark if it raised the discount rate or if the Committee made any deliberate change in its policy posture without overwhelming evidence of need.

Mr. Hayes said he wanted to make clear that he did not foresee a recession and was not suggesting that the public be warned about the prospect of one. In his opinion the domestic economy was doing very well but there was a lack of progress in the balance of payments problem. In fact, the situation appeared frightening when one looked back over the past five or six years. He thought monetary policy did have a role to play in connection with the payments problem, and that it was not possible to separate the question of domestic prospects from that of the international strength of the dollar.

Mr. Hickman said that figures now available for the second quarter reaffirmed the impression that the economy was growing at a balanced and sustainable rate. The preliminary figures on GNP showed gains of 1.6 per cent in both the first and second quarters. Industrial production, on a revised basis, showed a gain in the second quarter of 2.2 per cent, slightly larger than the 1.6 per cent gain in the first quarter. Retail sales, on the other hand, showed an opposite pattern, with sales up less in the second quarter than in the first (1.8 per cent as compared with 2.3 per cent).

The economic analyst could, therefore, take his pick as to whether the expansion was accelerating, decelerating, or steady. However, it was important to note that when the above increases for both quarters were summed and multiplied by two to obtain annual growth rates, the improvements thus far this year had been substantial:

industrial production was increasing at an annual rate of 7.6 per cent; retail sales at a rate of 8.2 per cent; and GNP at a rate of 6.4 per cent.

Expectations for continued gains in the economy were widespread, Mr. Hickman said, judging from views expressed at the latest meeting of 25 Fourth District business economists held recently at the Cleveland Bank. These economists felt that business would continue to expand, although not rapidly, during the next three or four calendar quarters. Doubts about the outlook were expressed only for the second quarter of 1965 and later, but primarily because of the low visibility of economic forecasts beyond the six-month horizon. There was widespread concern in the group about labor negotiations in the auto industry this year and possibly in steel next year. Incidentally, steel analysts in the Fourth District were now looking for a 1964 ingot output of 117-119 million tons, and automobile analysts were looking for an 8-million-plus car year. Representatives of both industries were now inclined to see total output for their respective industries next year as being below this year's record performance.

Scattered and incomplete reports for the Fourth District in July showed a rather mixed picture, with some signs of hesitation, Mr. Hickman continued. Part of the hesitation reflected the usual summer vacations and shutdowns, and part reflected a leveling that had occurred in iron and steel and the transportation industries in recent

weeks. The latest employment statistics for major labor market areas of the District, seasonally adjusted, showed three improvements, six declines, and five with no change. This contrasted to the situation earlier this year when changes were almost uniformly on the side of improvement.

With respect to monetary policy, Mr. Hickman thought that because of the imminent Treasury refunding the Committee was faced again with the need to maintain an even keel. He hoped personally that in following this course the Committee would not again experience the violent expansion in the money supply that had occurred recently. Between the first half of May and the first half of July, as the staff report pointed out, the money supply expanded at an annual rate of 9.3 per cent. In his opinion such an expansion hardly seemed consistent with an even-keel policy.

Mr. Hickman continued to feel that monetary policy had been too easy too long and that the Committee was building up serious problems for itself in the future. History seemed to show that if rates of monetary expansion similar to those that had prevailed in the recent past were continued for too long, they were likely to result in price inflation, boom, and bust. From the balance of payments standpoint also, excessive credit expansion and credit availability appeared to have encouraged capital outflows from both the banking and nonbanking sectors.

Mr. Hickman thought that as soon as the Treasury's calendar permitted, the Committee should push the bill rate to the general area of 3.60 per cent; and, in the meantime, it should continue to swap key foreign currencies, buying British pounds and Canadian dollars spot and selling them forward, to reduce or eliminate the covered yield differentials. He would also let the Canadians and the British know what was being done and why, and solicit their cooperation.

The revised draft directive was satisfactory to Mr. Hickman.

Mr. Bopp said that business continued to be good in the Third District. Labor force developments since the last meeting had been mainly favorable. Output, which wavered a bit in May, appeared to have picked up again in June. Sales at retail had been satisfactory, although not matching national increases.

Unemployment claims in Pennsylvania and Delaware continued to be low, compared with the totals of recent years. Help-wanted indexes increased in June in Philadelphia and the Middle Atlantic States, as well as in the nation. Unemployment rates typically decreased in June, although in a few places insured rates went up somewhat. The Third District now had no labor markets classified "F" and only one-- Scranton-- in the "E" category.

Electric power consumption and employment in the manufacturing industries of the Third District decreased more than seasonally in May, but both measures appeared to have recovered in June, Mr. Bopp noted.

This assessment was based on not quite complete data, however. Construction contract awards in the Third District this year were holding at last year's levels, as were national construction awards. Department store sales in the District were up 8 per cent over 1963 for the year to date, 9 per cent in the latest four weeks, and 6 per cent in the latest week.

Since the Committee's last meeting, Mr. Bopp said, reserve pressures on Third District member banks once more had increased and loans continued to better the year-ago performance. The basic reserve position of reserve city banks had shifted to the deficit side again after having been positive during the last two weeks in June. For the three weeks ending July 22, the deficit averaged almost $50 million. Borrowing at the discount window, both by reserve city and country banks, continued to be quite light.

Net loans adjusted at weekly reporting member banks rose by $17 million, compared to a year-ago decline of $1 million. Business loans dropped slightly but by an amount less than last year. Total deposits adjusted in the first half of July rose by $41.0 million, compared to a $70.1 million decline last year. The increase was predominantly in the category "other demand deposits adjusted," with time and savings deposits and interbank deposits also rising.

Mr. Bopp commented that as the economy passed the mid-year mark, it continued along a path characterized by steady expansion without

inflationary or speculative excesses. Perhaps most indicative of this course was the 5 per cent increase in gross national product over the second quarter of a year ago, coupled with a continued rise in output per man-hour in manufacturing and steady wholesale and industrial prices. In short, economic policy in the first half achieved the goal of steady growth without inflation, although there was still some way to go in attaining the objective of reasonably full employment of manpower and other resources.

Because of this general under-utilization of resources, Mr. Bopp regarded as a favorable development the steady growth in bank credit, in the money supply, and in other liquid financial assets. The question remained, however, as to whether this build-up represented inflationary tinder for the second half of the year. In a complex industrial economy, of course, anything was possible. Yet, in his judgment, ample unused resources rendered such a development unlikely.

As for the balance of payments, it was heartening to see the second quarter deficit revised a bit in favor of the U. S. It also was suitable that short-term rates had risen above their monthly lows.

In short, for domestic reasons, Mr. Bopp felt that the present posture of ease continued to be appropriate to the near-term future even in the absence of need for an even-keel policy to facilitate present Treasury financing. The present posture also was appropriate to the current balance of payments condition, although that condition

had to be watched closely during the remainder of the year. In his opinion the draft directive submitted by the staff was appropriate.

Mr. Bopp said that he might mention that there seemed to be a significant and rapidly increasing restiveness with respect to Federal Reserve membership in the Third District, particularly on the part of small and medium-sized banks. Some were actively considering withdrawing from the System. To some extent this situation was peculiar to Pennsylvania, where State banking laws gave significant competitive advantages to nonmember banks.

Mr. Daane entered the meeting at this point.

Mr. Bryan commented that he had no new and immediately current Sixth District figures that had not heretofore been presented. The economy of the District appeared to be robust as judged by directors' reports, and if judged by new plant and expansion announcements, would continue in good health for some time.

Borrowings from the discount window for some weeks had been generally heavier than seemed appropriate in view of the District's total banking resources as a proportion of national banking resources. But charts on member bank borrowings, over a longer term, exhibited an alternating pattern, first going above the 6 per cent line representing the District's relation to the national total of reserves, and then going below. He was thus unable to attach any particular significance to the present situation.

The national economy, speaking wholly to the domestic side, seemed to be going ahead nicely, Mr. Bryan said. The development did not at the moment appear to give clear indications of inflation; on the contrary. The development also seemed to be sufficiently balanced and symmetrical so that he did not see any present and compelling reason for believing that the national economy would shortly change its direction.

The money supply and reserve supplies seemed to Mr. Bryan to be in order. Accordingly, speaking to the longer run of three or four months, he believed that the Account Manager should aim for approximately a 3 per cent growth in total reserves after allowing for seasonals. In the shorter run, taking account of the fact that the Treasury operations would largely inhibit any change in policy, which in any event did not seem to be indicated, Mr. Bryan believed that the Account Manager should aim on a daily average basis for $100 million free reserves, plus or minus $50 million or so.

Mr. Bryan noted that he had not spoken of the balance of payments situation, but in his recommendation for short-run policy and longer-run policy had abstracted from the balance of payments for reasons that he had mentioned at other meetings. He would say, however, that in his judgment the balance of payments problem was extraordinarily serious, to the point that it might eventually force national policies resulting in a shock to the domestic economy. Without in any degree making a

forecast, Mr. Bryan said he could imagine a hypothetical, but quite possible, chain of events that might at some point lead to devaluation of the dollar. The problem here, Mr. Bryan said, was one of remedies. If it could be shown that monetary expansion in this country was primarily responsible for the balance of payments difficulties he would, of course, agree that the Committee must take primary responsibility in effecting a remedy. But he did not believe that this could be demonstrated.

Mr. Bryan said that he would not change the discount rate at this time. He was agreeable to the directive proposed by the staff.

Mr. Bryan then said that he would like to make a comment with regard to the staff's regular report to the Committee, "Current Economic and Financial Conditions," which was familiarly referred to at his Bank as the "green book." He thought the staff should be complimented for this book; its format and content were excellent, and he found it most useful. He wanted to raise a question concerning this report without having any firm convictions about the answer. On three or four occasions the Committee had discussed the possibility of publishing from time to time, in the Federal Reserve Bulletin or elsewhere, a review of economic developments and a statement about monetary policy. He had not reviewed the green book to determine whether there would be a problem in connection with confidential information, but the question that occurred to him was whether this book could be publicly released after each meeting.

At a minimum, this would make the most recent figures available promptly, and it would also indicate the variety of considerations the Committee had in mind at each meeting. Publication of this material might serve as a substitute for the types of articles the Committee had discussed on earlier occasions.

Mr. Shuford commented that economic activity in the Eighth District had continued on a high plateau since January. Perhaps it could be said to have inched up slightly, but generally speaking there had not been much change since the first of the year. Employment, bank debits, and department store sales remained at about their January levels. Bank deposits had continued to increase at a rapid pace, however, and business loans had risen markedly since April.

District construction activity had been at an advanced level in recent months, with contract awards so far this year 30 per cent above the same period a year ago. The sharpest increase had been in non-residential construction, but there also had been a substantial rise in residential building permits.

Farm crop prospects were good, Mr. Shuford said. The acreage planted to major crops was about the same as last year. Crops generally were in good condition for this time of the year, but, as had already been mentioned, it was a little early to be making predictions. Most of the small grains had been harvested and corn, cotton, soybeans, and tobacco were progressing satisfactorily. Dry weather in the southern

part of the District had been a problem, but recent rainfall had improved conditions. Livestock prices were below year-ago levels, but they had recovered somewhat from the depressed levels of April and May.

Nationally, Mr. Shuford continued, economic activity had continued strong in the second quarter. Output, employment, incomes, and retail sales all had increased significantly from the first quarter to second. The economy not only appeared to be healthy, but it also was strong in all major sectors. Inventories were not excessive, and at this time there appeared to be no major imbalances.

There had been considerable churning in the money and capital markets during the past two or three weeks, Mr. Shuford noted. As Mr. Noyes had anticipated at the last meeting, shifting from "rights" into Treasury bills in connection with the advance refunding had put Treasury bill rates under downward pressure, but after the refunding rates returned to the levels that had prevailed since last November. Pressures in the money market, as reflected by data on Federal funds rates, dealer positions, free reserves, and the like, changed little on balance. The most recent data on bank reserves, bank credit, and the money supply showed marked expansion. However, since late last year monetary growth had been in the 3 to 4 per cent range. Mr. Shuford noted that in the latter part of 1963 the Committee had been concerned about the high rate of growth in the money supply, and a few meetings

ago it had been bothered by the fact that the growth rate then was quite low. Now the growth rate was back up again. It behooved the Committee, Mr. Shuford said, to consider the behavior of the money supply from a longer run point of view.

Mr. Shuford commented that the balance of payments problem continued to be troublesome, and increasingly so at present. For the time being, however, he favored no change in policy for the various reasons that had been discussed, including Treasury financing activity. The staff's draft directive appeared satisfactory to him.

Chairman Martin noted that Mr. Daane, returning from a trip abroad, had joined the meeting a short time earlier, and he asked whether the latter had any comments.

Mr. Daane said he thought no change in policy was called for, particularly in light of the recent surprisingly successful advance refunding, and of the imminence of further Treasury financing activity. He had been somewhat confused by the available data on balance of payments developments, and he felt this was an area that the Committee should watch carefully. At this juncture, however, he thought no change in policy was the best course.

Mr. Balderston commented that at the moment the market might need to be let alone to digest the large volume of Government securities issued in the recent advance refunding. Since the redistribution of the dealer and other temporary holdings should not take long, it was

his hope that the Committee would use the interim to take a fresh look at the current posture of monetary policy with a view to minimizing the outflow of dollars at present and a possible resumption of gold outflows in the future.

Fortunately, Mr. Balderston said, the Committee was now approaching a period in which some adjustment of that posture would be possible. He therefore would address himself to what might be called "a stitch in time." In favor of some gradual lessening of the pace of bank credit expansion were several considerations:

First, the rate incentive for American corporations and banks to place funds abroad needed to be diminished in view of the balance of payments outlook. He was impressed with Mr. Deming's comments on movements of corporate funds to Canada. Actual rate advances in Europe, coupled with the expectation of others, had induced nervousness that could increase. While the long-term claims on foreigners reported by banks increased in the second quarter by only $70 million, Mr. Balderston suspected that this reduced figure was not representative of the outlook for the year as a whole.

Secondly, Mr. Balderston continued, although traditional relationships did not indicate a significant increase in corporate liquidity ratios, it was clear that big corporations had large and growing quantities of liquid funds. Consequently, they would continue to cast around for opportunities to employ this liquidity, including placement of funds overseas.

In most European countries except Germany, both short- and long-term rates since a year ago had advanced by about enough to offset the rate increases in the U. S. during the same period. Currently, the 4-1/2 per cent prime rate in the U. S. was lower than that in any of these countries except Switzerland, and in that country banks had had to become more selective in lending at that rate.

The final consideration, Mr. Balderston said, had to do with liquidity of individuals, which continued to mount as a result of the high rate of saving and the fact that bank loans and investments had grown at a fast pace, averaging about 8 per cent annually since early 1961.

The money supply had increased markedly since mid-May, at an annual rate of 9 per cent--a rate that should not be sustained. And so at a time when European countries, excluding Sweden and Britain, had cut their rates of money supply expansion, the United States had continued to provide comfortable bank credit availability. The important factor was that stiff restraint in Europe and no restraint here would tend, over a period, to bring to a halt the recent improvement in the relative competitiveness of U. S. business and in the payments deficit.

Mr. Balderston commented the U. S. balance of payments problem could not be solved by any one action, as others had remarked earlier in the meeting. But since other developed countries were taking steps

to counter present and developing inflationary pressures, and the business situation here remained steadily strong, he thought it would be appropriate to consider shifting System policy shortly to induce more discounting by member banks, especially the large city banks. The need for some action was reinforced by the growth of nonborrowed reserves in the first half of this year at an annual rate of 5.9 per cent. If this were done, one could not foretell whether or not the big banks would give preference to domestic rather than foreign lending, but it was worth a trial. It was more certain that some increase in bill rates would reduce the incentive for bankers and nonbankers to place funds abroad.

To focus this argument upon a concrete proposal, Mr. Balderston said, he favored rates of upward of 3.60 per cent for the three-month bill, but not above 3.75 per cent for the six-month bill. Further, he would probe to discover the effect of forcing a somewhat higher volume of bank advances at the discount windows. To achieve both of these ends would require letting free reserves move close to zero, and even below zero.

Since his concern, Mr. Balderston said, centered upon some redressing of bill rates without setting off too large a shrinkage of negotiable CDs, and upon staunching any future gold outflows, he was inclined to the view that a change in reserve requirements might be used again this fall, as Mr. Hayes had suggested at a previous meeting.

Used instead of the open market instrument, it would meet seasonal credit needs without depressing bill rates and, equally important, it would reduce the gold requirement. It seemed to Mr. Balderston that unless action was taken early enough, the action that would be required later might have to be more drastic than he would consider desirable.

Chairman Martin commented that he thought the consensus was clear today: an even keel policy should be followed during the next three weeks. Some members would prefer that any minor deviations be on the side of firmness; others would evidently prefer that they be on the side of ease. He added, with a smile, that his own suggestion would be not to have any errors at all. The Chairman also commented that the suggestion for consideration of a change in reserve requirements deserved careful study.

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

It is the Federal Open Market Committee's current policy to accommodate moderate growth in the reserve base, bank credit, and the money supply for the purpose of facilitating continued expansion of the economy, while fostering improvement in the capital account of U. S. international payments, and seeking to avoid the emergence of inflationary pressures. This policy takes into account the continued orderly expansion in economic activity, accompanied recently by a more rapid

expansion in money supply and little over-all change in interest rates. It also gives consideration to the relative stability in average commodity prices; the underutilization of manpower and other resources; the apparent deterioration in the international payments balance in the first weeks of July; and the interest rate advances in recent months in important markets abroad.

To implement this policy, and taking into account Treasury financing activity, System open market operations shall be conducted with a view to maintaining about the same conditions in the money market as have prevailed in recent weeks, while accommodating moderate expansion in aggregate bank reserves.

It was agreed that the next meeting of the Committee would be held on Tuesday, August 18, 1964, at 9:30 a.m.

Chairman Martin then suggested that the Committee give consideration to the memorandum dated June 16, 1964, from Messrs. Ellis, Mitchell, and Swan regarding the Committee's current economic policy directive. He asked whether the authors of the memorandum would care to comment.

Mr. Mitchell observed that the memorandum in question had been in the hands of the Committee for about six weeks, and that it had been discussed at a staff conference in San Francisco during the preceding week. He would make only two points. One was a point he had made when the report was first presented: that while the proposal in the memorandum was quite specific, the authors had not intended to be dogmatic. The proposal reflected the authors' best judgment as to how it might be most useful to start what could be termed an experiment. But the

specifics could be modified readily, and it was contemplated that they would be changed informally and gradually. If the Committee did decide on changes, they could be accomplished without inconvenience.

For himself, Mr. Mitchell said, he felt a certain sense of humility in setting this proposal before the Committee, but he was not diffident about it; he thought it important to try to improve the techniques used in wording the directive.

Secondly, Mr. Mitchell said, he wanted to comment on one type of criticism of the proposal that he had heard, namely, that the procedures suggested would increase staff responsibilities considerably. It should be noted, he said, that under the proposal Committee members' work also would be more difficult. It was the effort to be more specific that increased the burden. Moreover, Mr. Mitchell said, the purpose of the elaborate and expensive apparatus for economic reporting and analysis which the Federal Reserve System maintained was to provide the basis for a flexible countercyclical monetary policy. Such an apparatus would not be needed if the System were to follow an automatic policy such as some recommended, under which reserves would be injected at a constant rate.

Mr. Mitchell thought the directive should show not only what actions the Committee was taking but also how it analyzed the economic situation and what its prognoses were. There were many uncertainties and gaps in the Committee's knowledge, and because of them the proposals

in the memorandum might seem to be lame and halting, he said, but he commended them to the Committee as a step in the right direction.

Mr. Swan commented that he had little to add to what Mr. Mitchell had said, and would simply point out to the Committee what he personally considered to be the two most important sentences in the report. One, which occurred near the bottom of page 12, read: "However deficient the state of the art, the Committee must, and now does, make judgments of the sort that would be required under the proposal." This thought was worth bearing in mind. The other was the last sentence of the text, on page 13: "In the effort to face the issues directly the Committee and its staff undoubtedly will come to have a sharper understanding of the problems, and this alone would be a long stride toward solutions." Mr. Swan expressed the hope that if the Committee moved in the proposed direction it would not only improve its own processes and directives but in the longer run it would also improve some of its basic research programs and facilitate improvement of its analysis of many of the issues involved.

Mr. Ellis said the three authors of the report had found they had a high degree of uniformity in their approach to the problem of the directive. They had not had the advantage of Committee discussion of the Secretariat's memorandum of April 8, 1964, which appraised existing directive procedures. Their own memorandum, in effect, started with a judgment of the three authors with respect to the present practice, and

they were not sure how widely that judgment was accepted among the Committee members. However, the authors made an assumption that the Committee did share their judgment, and they then attempted to set out a modest but significant step toward improvement of the directive. The central point of their report was the suggestion that the Committee should establish priorities among its objectives in terms of economic series that were measurable and that could be used to set targets and goals in numerical form.

The Committee might well disagree with the specific choices made in the report, Mr. Ellis said, but the overriding questions were whether the Committee itself should decide on priorities and whether it should express them in measurable magnitudes. If the Committee agreed that it should do both, the question was where to start. The authors were quite tentative in their suggestions for a starting point.

Chairman Martin commented that despite his skepticism, which had not been completely removed, as to whether too much could be done in this area, the Committee had an obligation to make its directive as realistic and intelligent as possible. While the suggested procedure would make more work for both the Committee and the staff, as Mr. Mitchell had indicated, this was no reason of itself to shirk the effort.

The Chairman then called for comments around the table, and Mr. Hayes made the following statement:

The memorandum before us, as well as the earlier memorandum prepared by the Secretariat, has made a signal contribution to the discussion of the Committee's economic policy directive as a means for instructing the Manager and communicating with the public. I think all of us have felt that our responsibilities for the conduct of monetary policy demand nothing less than our utmost efforts to instruct the Manager as clearly as possible in achieving the Committee's objectives, and in informing the public as clearly as we can as to those objectives and instructions.

At the same time, I do not believe it would be wise for the Committee to adopt the present proposal for quantitative monetary objectives and detailed quantitative instructions. Given the current inadequate state of our knowledge about financial processes, and their linkages with real economic activity, I am especially dubious about the suggestion to single out a particular monetary variable and specify a particular growth rate for that variable as the System's primary policy objective. It would be presumptuous to expect that our directives could resolve the issues that have confronted monetary theoreticians and policy makers for so many years, and I do not believe that a good directive need attempt this. An effort to impose this task on the directive will neither contribute to public understanding nor to the quality of policy formulation. I would be the last to say that our directives are incapable of improvement, and I would like to make a few comments on this later. However, I do not share the feeling of serious dissatisfaction with the existing directives that underlies these new proposals. It seems to me that for the most part the existing procedure works well, and I see no merit in substantial change unless the change brings very real advantages. It is also my impression that most members of the Committee have been generally satisfied with our existing procedure.

Turning to the specific proposals, it seems to me that there are real dangers to the quality of the Committee's decisions if it tries to reach agreement every three weeks on so comprehensive and complex a document as the proposed directive. Given the difficulty we frequently have in agreeing on wording in the present much simpler directive, I do not see how the proposed procedures for developing the new directive would prove workable unless we limited ourselves merely to choosing among alternative drafts prepared by the staff. Inevitably, this would mean delegating

important judgments which are the appropriate province of the Committee itself.

I have some difficulty on this score even with regard to the least controversial of the proposed directive's components--the analysis of recent business and financial developments in Elements 1 and 2. At present, the "policy record" has the benefit of being drafted after an interchange of views among Committee members at our regular meetings. Moreover, members have an opportunity to suggest changes before the record is put in final form, and I believe that useful improvements often emerge from this process. In contrast, the new proposal would in all practicality require that a distilled analysis of recent developments be prepared in advance of each meeting and before each member's views and the Committee staff's comments had been heard and weighed. Since this analysis would provide the foundation for the statement of the Committee's policy intent and specific operating instructions, Committee members could hardly pass over lightly the selection of data made by the staff or the interpretations placed upon the data. Yet I doubt whether we are often in such close accord on the factors to be emphasized that we could agree quickly on an official analysis rationalizing the group's policy prescription. Too many substantive issues are involved.

Moving on to Element 3 in the proposed directive, the statement of the Committee's policy intent, I am extremely dubious of the proposal to make a specific percentage rate of growth in reserves behind private demand deposits the Committee's primary policy objective. I do not believe that our knowledge of the dynamics of the interaction between reserve expansion and economic growth is so well developed that we can fix on a single measure as the target for monetary policy--whether it is private demand deposits, money supply, bank credit, or one of the aggregate reserve measures. And to select not only a particular measure but also a specific desired growth rate seems daring indeed. All of us sitting around this table are well aware that the linkages among monetary variables may change as our economy develops. To endorse a single policy variable may satisfy an urge for theoretical neatness, but it represents in my view a potentially dangerous retreat from the real world. Pursuit of the particular measure mentioned in the present proposal--private demand deposits--would seem to slide over all the questions we have had about how to interpret the

very rapid growth of time deposits and all the uncertainties associated with sharp changes in the level of Treasury deposits. It would also gloss over the very substantial month-to-month variability in these measures--variability in which a month or two of substantial gains might be followed by sharp swings to contraction or vice versa.

I am concerned also with the attempt under Element 3 to specify particular expectations about interest rates or credit conditions that we would associate with the reserve growth goals. This would seem quite premature, given the current state of knowledge. Certainly before we can contemplate an approach of the kind proposed in the memorandum, there must be a great deal more study of our financial processes, and the linkages between those processes and the performance of our economy, domestically and internationally. And even then, without venturing to prejudge the results of this needed research, I wonder if we could hope to rely on simple fixed targets of the kind mentioned in the memorandum before us. One obvious qualification that comes to mind is that if, at times, the Committee should address its policy particularly to our international position, this may not lend itself at all to expression in terms of a desired growth rate in one of our reserve measures. Rather, the principal emphasis then might appropriately be placed on general market conditions.

As for Element 4, I believe that the Committee should continue to instruct the Manager in qualitative rather than quantitative terms. I am not only dubious of the Manager's ability consistently to hit quantitative targets such as a range of $50 million to $150 million average free reserves, but I am also concerned lest an effort to hew more closely to such targets lead to considerably wider fluctuations in money market conditions. In particular, the choice of a free reserve target would strongly reinforce the position of those observers who grossly oversimplify and regard free reserves as the be-all and end-all of monetary policy. We have made considerable progress in recent years in breaking down the market's preoccupation with free reserves. It would be unfortunate to retrogress by specifying a range or a central value for free reserves as our target.

If the specified ranges are narrow enough to indicate a measure of precise control by the Committee, the variables are likely to fall outside the prescribed ranges quite often. An occasional failure to hit the Committee's targets would be understandable and readily explained, but I wonder if frequent departures from the targets would not be taken as prima facie evidence that the Committee does not effectively control the

execution of its policy. Of course, the target ranges specified in the directive could be widened to the point where there were few misses, but in this case I wonder how meaningful the quantitative instructions would be. From the standpoint of public consumption, a wide range would only point up an apparent lack of precision in the Committee's instructions to the Manager, leaving an implication that the Manager must have some other guides by which to operate.

On the other hand, I would see no objection at all to individual Committee members mentioning quantitative objectives as they make their comments and recommendations on policy at each meeting. As a Committee member I find such references useful in organizing my thoughts, and I believe the Manager finds them useful in applying the Committee's decisions at the Desk. It would also be useful for the public to know that the members of the Committee at times use quantitative terms in expressing their views. But rather than have this embodied in the directive, with all the rigidities that this would tend to impose, it would be much preferable for the interested public to become aware of this practice through the minutes for 1936-1960 that are now being opened to public perusal.

To consider more specifically how the formal detailing of targets or target ranges would impair the functioning of monetary policy, one might envisage a situation late in a statement week when the market tone seems about right but the projected reserve average is higher than the Committee has called for. Close pursuit of the target would require substantial sales of securities, perhaps to be followed shortly by substantial purchases if the sales were depleting reserves too sharply for the following period. The result might well be more frequent and larger System operations, with no apparent relation to the money market atmosphere. Inevitably, System actions would appear arbitrary and capricious to the market, tending to undermine the continuity of money market atmosphere that is an important ingredient in the smooth functioning of the financial mechanism.

The disadvantages of spelling out in the directive the Manager's required response to changing circumstances are also evident in the subsidiary instructions relating to the Treasury bill rate. If a 3.40 to 3.55 per cent range is specified for the 3-month bill rate, does this mean the Manager is to take no action until the rate reaches 3.40 per cent? And is his only response to be to curtail free reserves? I wonder if

better results are not likely to follow from having the Manager not merely respond in Pavlovian fashion to a particular rate level, but weigh the momentum of a trend in rates, and perhaps set in train a series of responses as rates move downward--or at other times, when the rate decline seemed clearly temporary, having the Manager refrain from special action addressed to the bill rate and permit natural market forces to bring about a reversal. This would seem to be more in line with the Committee's desire to have rates as free to move as possible rather than boxed in by rigid limits. Indeed, the insertion into the directive of specific rate targets, and the market's eventual knowledge of that fact, would have a highly rigidifying effect on rates.

In summary, while I feel a good deal of sympathy with the objectives of these proposals--that is, the presentation of an integrated rationale of the System's policy intent and of operating instructions that would be more meaningful to the public--I feel that the proposals before us are just a starting point toward these ends. As such, they have performed a very useful function in stimulating thinking on possible improvements in our directives. My own thoughts in this area are still quite tentative but I might just mention a few of the areas that my colleagues and I have been considering. First, it might be desirable to make greater use of judgmental-type statements in those parts of the directive relating to recent economic and financial developments. The directive might, for example, give a clearer indication than at present whether there has been an improvement or deterioration in the situation, whether recent developments have borne out prior expectations, and to what extent money market conditions have developed along lines sought by the Committee.

Second, a clearer distinction might be made between the Committee's assessment of the economic situation and outlook on the one hand, and its general policy posture on the other. Thus at times, the Committee might note that while business had strengthened and the outlook had improved, a change in policy was not desirable because of continued unemployment.

Third, we might be more explicit about expected and desired behavior of credit markets and key financial indicators for several months ahead, making it clear that our time horizon extends over that intermediate range and is not confined to three-week intervals. I should add, however, that even rough attempts to set down our expectations are subject to some dangers, and certainly will remain so until we know much more about the underlying linkages. All these lines of thought

> deserve and require further study, but in the meantime let us not abandon a procedure that has proved workable and has yielded what seem to me quite satisfactory economic results.

Mr. Irons said that he had found the memorandum interesting and stimulative, and that he intended to study it further. The more he had considered it, the less strong were his reactions, but he did have qualms about certain aspects of the proposal. His thinking started with the assumption that what the Committee needed was a directive to the Account Manager that would be understandable, capable of being carried out, and accurate in reflecting the policy posture of the Committee. He placed less emphasis than some others on the role of the directive in informing the public, which seemed to him to be one of the considerations underlying the proposal that the Committee had before it.

Mr. Irons thought that the Committee had a fairly satisfactory way of informing the Account Manager of the Committee's policy posture in its present directive. The Account Manager was continually responsive to the Committee. If, during the three-week period, he did not perform as Committee members thought he should have, they had an opportunity to criticize his operations at the next meeting.

Mr. Irons noted that element 4 of the illustrative directive attached to the report began: "To implement this policy, System open market operations over the next three weeks shall be conducted with a view to maintaining weekly average free reserves in the $50-$150 million

range." This instruction specified positive numbers, which would be published later, and the Manager would have to try to hit the target given. There was no provision in this instruction for the tone and feel of the market. However, the next sentence of element 4 seemed to undo what was done in the first sentence. It read: "Provided, however, that free reserves should be permitted to move above or below this range in order to moderate any movement in the Treasury bill rate outside the range of 3.40-3.55 per cent or any serious constriction or excess in the availability of Federal funds or dealer financing." Thus, although an initial priority was set up, it was a weak priority.

Mr. Irons said that he was fearful of using in the directive quantitative measures of which the Committee was not sure. There was a difference, in his judgment, between specifying a range of figures intended to apply if other things were equal and naming a range of figures that must be met regardless of other circumstances. He was not concerned about references to quantitative targets in the Committee's deliberations, but he would be concerned if such targets were to be spelled out in a directive that would be published later. While some might have only a hazy impression of what was meant by the words "tone and feel," he thought these words had real meaning to the Manager, who was in the midst of market operations and who had a sense of the developments occurring in the market at any given time. Mr. Irons thought it would be a mistake to divorce the Manager from considerations

of tone and feel, and to hold him to quantitative targets. Moreover, if the Committee issued quantitative instructions, it probably would find that more frequent operations in the market were required, as Mr. Hayes had suggested.

With respect to elements 1 and 2 of the proposed directive, Mr. Irons said, the Committee now was providing, in the policy record, much of what the report recommended. The content of these elements seemed to be simply a revised version of the forepart of the policy record entry, where recent developments were reviewed. Mr. Irons questioned the desirability of expanding the directive to include what basically was background information at the time of its adoption. The Committee was given such information prior to each meeting in the "green book" and in other memoranda. This kind of information underlay the Committee's thinking and analysis, its policy conclusions, and its instructions to the Manager, but he did not believe it would be desirable to make it a part of the directive. He would be interested in giving more background material to whoever wanted to read it, and in this connection he would be quite favorable to considering the possibility of making the green book available, as Mr. Bryan had suggested. If the Committee moved in the direction proposed in the report, however, it might get into the same kind of difficulty that had arisen in connection with the preparation of detailed minutes. He thought, also, that the Committee would be making trouble for itself if it attempted to include

in the directive an extensive statement of the facts it had considered. The directive almost had to be written in relatively general terms if the Committee was to get its job done effectively. Avoiding highly specific instructions did not mean that the Committee could not hold the Manager accountable for his operations.

Summing up, Mr. Irons said, he strongly questioned the desirability of introducing quantitative targets into the directive, and he questioned whether the Committee would achieve much from the first two elements of the proposal that was not already accomplished through the policy record entry and in other ways. He had one other point, in connection with which he was somewhat disturbed by present practices. That was the question of delegation of responsibility by the Committee to its staff, particularly in connection with the preparation of draft directives for Committee consideration. The proposal would magnify this problem considerably, he thought. The report recommended that the staff distribute, before each meeting, drafts of the first two elements for Committee review, and background material to facilitate preparation of the next two elements by the Committee. But drafting of elements 3 and 4 around the table might well be found to be quite a chore; and it was likely that the next step would be for the Committee to have the staff draft these elements also.

Mr. Irons thought the Committee should give serious consideration to better methods of informing the public; he was sure all of the members would favor that. Publishing the green book was one possible approach. Another that had been suggested on several occasions was to publish a quarterly review in the Federal Reserve Bulletin which would spell out the nature of developments and of the Committee's actions in the preceding quarter. Such a procedure was followed in a number of other countries. It would accomplish the objective of informing the public better without disturbing the Committee's basic working instrument--its directive to the Manager of the Account.

Mr. Deming commented that his views were similar to those of Mr. Irons, except that he did not share the latter's concern about the staff's role in drafting directive material. He thought the Ellis-Mitchell-Swan memorandum had made a notable contribution to the continuing discussion about Committee procedure and the nature of the directive to the Desk. However, he took fairly sharp issue with two of the basic conclusions of the study.

In his view, Mr. Deming said, the positive contribution came from the sharp focus on certain points that needed thorough consideration, from suggested procedures which should aid Committee discussion and minimize inconsistencies in instructions, and from the almost explicit recommendation for extensive research on linkages between proximate, intermediate, and ultimate objectives of policy. His

disagreement, like that of Messrs. Hayes and Irons, was, first, with the length and complexity of the suggested form of directive and, second, with the recommendation to quantify, too precisely in his view, certain of the long-range objectives of policy and, more particularly, certain of the short-term guides.

The suggestion for staff provision of background material for all four elements of the group's suggested form of directive was excellent, Mr. Deming thought. This should help a great deal in minimizing inconsistencies in instructions. He would suggest one additional step in this procedure, which perhaps was implicit in the proposal. This would be a quarterly review and "look-ahead." The review would compare actual performance of the intermediate and ultimate variables with what seemed to be desirable or with what the Committee had hoped to attain. The look-ahead obviously would involve some forecasting, or at least the statement of certain objectives, but Mr. Deming thought it would be of benefit to the Committee. In a sense the Committee already did some of this; the suggestion really came down to a more formal approach.

Mr. Deming thought the memorandum's reference to the urgent need for research was something the Committee should clearly keep in mind. While he was not particularly sanguine about the probability of establishing very precise linkages among proximate, intermediate, and ultimate objectives, the Committee should explore this field far more thoroughly than it had.

Finally, Mr. Deming said, the report should be commended for its sharp focus on certain issues involved in procedure and directives. The authors had performed a signal service in getting their points down on paper, whether or not the Committee agreed with them.

Turning to his areas of disagreement, Mr. Deming said he thought the proposed directive was far too long and too complex. He doubted that the directive could be made a public relations document; another vehicle was needed for that purpose. Extended discussions at meetings probably would be necessary to reach agreement on a directive of the length proposed. This would be particularly true if the drafts included as many polar words as did the illustrative directive for May 5. In the past he had been on both sides of the question of the desirable degree of complexity in the directive. At present he leaned toward simplicity, and toward the preference that Mr. Mills had expressed on several occasions for something along the lines of "clause b" of the type of directive the Committee had issued before December 1961.

Mr. Deming agreed with Mr. Irons that the proposed content of the first two elements was more properly a part of the policy record than of the directive. At the most he would include a simplified version of this material in the directive, somewhat along the lines of the present directives.

On the matter of quantifying instructions, Mr. Deming thought the points made by Mr. Irons were valid; any member was free to mention

quantitative goals in the course of discussion at present, and the Manager could be held accountable for conformance with the instructions given him. To include numerical instructions in the published record, Mr. Deming believed, would lead to a great deal of capricious and uninformed criticism of the Committee, particularly in view of the magnitudes of the revisions in the figures. Moreover, as the memorandum pointed out, the Committee might not always want to use free reserves for specifying its targets.

In sum, Mr. Deming said, he thought the procedural suggestions in the memorandum were well worth consideration; they would sharpen the Committee's focus on policy questions. But he would favor keeping the directive simple, and avoiding quantification both in instructions to the Manager and in statements of longer run policy intent.

Mr. Helmer said he had no comments on the memorandum.

Mr. Tow said that in his judgment the idea of moving toward a more comprehensive and more explicit directive was a very good one. Implementation of the recommendations in the memorandum under discussion would bring a number of improvements, but it also would create problems that would need to be worked out over time.

Mr. Tow thought the inclusion of element 1 on economic developments and element 2 on credit developments would be important additions to the directive. This would result from both the more comprehensive description and the added analytical emphasis. Inclusion of these

sections, as possibly amended by the Committee in any given meeting, would provide a logical groundwork for the policy statements in elements 3 and 4. The principal question about including longer elements 1 and 2 in the official directive was the ability of a Committee of 12 people to agree on the wording without becoming bogged down in too much discussion of detailed phraseology.

The biggest change from the present directive, Mr. Tow noted, was the inclusion of element 3 as a statement of the Committee's longer run policy intent. A more specific statement of longer run policy intent would be a constructive step, in his view, although the inclusion of this section also would create some problems to resolve. One problem would be that of internal consistency, arising from the different approaches to monetary policy taken by Committee members. Some preferred what might be called a credit and interest rate approach, while others preferred some variant of a money supply approach. Accordingly, it would be necessary to write element 3 in such a way that both approaches would be incorporated. To some degree, that had been done in the illustrative directive attached to the memorandum. This problem could not be avoided--if its avoidance required agreement on any one approach to monetary policy--but over time the problem should be lessened through increased knowledge concerning the relationships between these variables.

Another problem, Mr. Tow said, arose from the effort to quantify the targets adopted. No matter what measure was used, whether aggregate

reserves, money supply, credit, interest rates, or some other, there was no way of knowing what the correct quantification should be. Whether figures were used or not, however, the Committee had to observe what was happening to its ultimate economic objectives, and change these intermediate goals if and when necessary. Added research should enable the Committee to make better approximations in the future, but there could never be exact projections.

Whether quantification was used or not, Mr. Tow thought the inclusion of element 3 would be an important improvement in the Committee's directive. For the time being, it might be better to experiment with a verbal approach with a view to quantification later. In the interim, research, including work on quantitative models, could be carried on.

In his judgment, Mr. Tow said, quantification was the main issue in element 4, as the general framework proposed was essentially that used by the Committee at present. The question of what figures to use again was an issue, but in a somewhat different way, as changes could be made from time to time relative to the achievement of the goals set forth in element 3. There also was a problem of consistency among the short-run targets, but the draft provided escape provisions for various contingencies over the short interval between Committee meetings that should go far toward alleviating this problem. He did not think this element could be written with two or more variables

without escape clauses, since it was not possible to predict how the relationships among the variables would work out.

A leading issue, Mr. Tow said, appeared to be the impact on the market when the Committee and its Manager were committed to explicit quantitative guides. This was a difficult issue on which to pass judgment. Much might depend on how the matter was handled. The proposal did not call for any particular guides to be used indefinitely, but provided that different guides should be used, depending on what was most appropriate at any given time. Presumably the market would come to understand that it could not assume that any particular guide would be used indefinitely, let alone any particular guide values. There was reason to wonder whether the problems of the Committee and the Manager in connection with this matter would be any greater than they were now.

It seemed to Mr. Tow, however, that the most important issue before the Committee at this time was the adoption of the general framework for the directive that was proposed in the memorandum. He personally thought that adopting this framework, even though quantification was not accepted, would be a highly constructive step, and one worthy of consideration by the Committee. Quantification, whether or not adopted to some degree at this time, should be a continuing goal.

Mr. Wayne said that he agreed with most of the views that had been expressed by Messrs. Hayes, Irons, and Deming. He believed that the Committee's present directive was a distinct improvement over that used previously. He could understand the desire to arrive at some neat, clear model that would look well, but he was persuaded that a move at this time in the direction proposed would prove treacherous. His concern was focused by the thought that the Committee would have to experiment in quantifying targets and then verify in retrospect whether or not the quantity it had named was correct. To experiment within the official directive of the Committee to the Desk would invite criticism.

Mr. Wayne thought the report had served a useful purpose in focusing on the question of linkages in the economy, and he would consider it highly desirable for the System to do more research in this area. But to attempt to draft directives of the type proposed in advance of such research would, in his judgment, be dangerous. Instead, work designed to increase knowledge of linkages should be pressed first. He also shared the other concerns that had been expressed about quantifying instructions to the Manager.

Mr. Mills said he concurred in the views that had been expressed by Messrs. Hayes and Irons, and in some of the variations on these views expressed by other members of the Committee. He was suspicious of the target approach, feeling that the inevitable result would be to repeat

the history of religion, where simple faith over the years had been sacrificed to symbolized ritual without inspiring people in general. He thought that would inevitably be the path followed if the Committee adopted the proposals made. Their adoption would amount to a surrender to statistics in place of instinctive adaptation to circumstances as they developed.

Mr. Mills said he would much prefer the present directive to the kind proposed and, as the Committee knew, he was not happy with the present directive. He thought the first and second paragraphs were contradictory; the emphasis in the first negated what was called for under the second. As Mr. Deming had noted, his own preference would be to return to the old clause (b), a subsection of the type of directive the Committee formerly had used.

Mr. Robertson commented that he was grateful for the memorandum, because he would like to see a better job done with the directive, and he assumed the other members would also. However, he, too, quarreled with the particular proposals. It seemed to him that the first two elements were not properly sections of a directive at all; they covered ground that now was covered in the policy record, except that it was proposed to draft them in advance of the meeting rather than afterward. In his judgment the illustrative drafts of these elements did a better job than did the corresponding part of the present policy record entries, and he thought their format could be used to advantage in the record.

Moreover, while he did not think elements 1 and 2 should be made a part of the directive, he was not opposed to their preparation in advance of the meeting. In fact, he thought it would be desirable to have such information brought to the attention of the Committee before each meeting, so that there would be a clear understanding of the situation that had to be dealt with at that meeting.

Mr. Robertson also had no fault to find with the desire to set forth the policy intent of the Committee for a longer period than 3 weeks. But he was concerned about the risk of being too specific in a directive that would be published. He doubted the advisability of using precise numbers in either element 3 or element 4. In his judgment the directive should indicate the general kind of monetary climate the Committee was seeking. With respect to the use of a free reserve range in element 4, he doubted the wisdom of always using a free reserve range for instructing the Manager, although he knew of no better way of indicating what operations the Committee thought were necessary to achieve the results it desired. Moreover, he would strike the last sentence of element 3 relating to credit conditions. And in place of the subsidiary instructions of the type proposed for element 4, setting specific limits for the bill rate and describing money market conditions under which the Manager was authorized to deviate from his first instruction, he would substitute some such language as "in order to moderate substantial swings in money market conditions, and to partly offset any tendency of the

growth rate for required reserves behind private deposits (for example) to deviate substantially from the average rate of the past year." Such language would give the Manager authority to deviate from any specified free reserve range without requiring him to maintain the bill rate or other rate within any precise limits. The Manager would have to use judgment, but that was a part of his job.

Mr. Robertson expressed the hope that the Committee would agree on some lines along which it thought progress might be possible, and undertake to experiment with a directive on these lines for three or four meetings on a side basis. The experimental directives would not be officially adopted; the Committee would continue to issue directives of the present type. But by experimenting informally, the Committee would have an opportunity to check back after the fact, and determine whether it seemed feasible to develop more precise directives.

Mr. Shepardson said that elements 1 and 2 seemed to him to be more appropriately a part of the policy record entry than of the directive. On the matter of providing this type of material to the Committee before each meeting, he felt that such information was largely contained in the green book, which was available to the Committee prior to the meeting. In his judgment, the present type of policy record statement, which was developed on the basis of both information from the green book and the discussions at the meeting, was superior to the type of predeveloped statement proposed for elements 1 and 2. He thought

also that these elements would add unduly to the length of the directive, and he would prefer a more concise statement, such as was contained in the first paragraph of the present directive.

With respect to the details of the proposal, Mr. Shepardson felt that the fluctuations observed over time in the various quantitative series raised considerable hazards in trying to set forth numerical targets in the directive; they could be pointed to as targets that were more often missed than hit. In his judgment there were too many factors involved to permit the selection of two or three and the omission of others from the directive. Such a procedure, he believed, would open the gate unnecessarily to charges of "misses" that would not necessarily have been significant.

Mr. Shepardson said he, like others who had commented, was hopeful that through research a better understanding of the underlying relationships could be developed. At the moment, however, it was clear that the Committee did not have a full understanding of them. As he had mentioned at the preceding meeting, without any change in the objectives of the Committee or in the operations of the Desk, there recently had been marked fluctuations in the rate of growth of the money supply. The Committee had yet to develop a full understanding of the causes of such fluctuations, and until it did it was unnecessarily hazardous, in his view, to attempt quantification in the directive.

Mr. Shepardson said he favored making the type of material included in the green book publicly available. He noted that the Committee had made progress in getting its policy record entries prepared on a more current basis. This was an important improvement because it avoided the possibility of any suggestion that the entries were written with the aid of hindsight. The Committee still had not taken a further step, involving a more current release of the policy record entries--perhaps a quarterly release. He thought it would be desirable to accelerate the release of these entries. But he was skeptical about the extensive type of directive suggested in the memorandum.

Mr. Daane said he considered the proposed directive unnecessarily complicated. This was particularly true of elements 1 and 2, which, he thought, did little more than add window dressing to what was now included in the policy record. Moreover, staff resources were likely to be strained in the attempt to draft these elements in advance of each meeting, and the staff could spend an undesirable amount of time in worrying about specific language. In his judgment elements 1 and 2 should not be made part of the directive. Perhaps more thought should be given to improving the corresponding part of the policy record entries. With respect to the proposal to release the green book or some version of it, his initial reaction was favorable.

On element 3, Mr. Daane said he shared Mr. Hayes' question about the desirability of specifying the Committee's longer run policy intent in terms of the seasonally adjusted annual rate of increase in required reserves. He recalled a discussion by Mr. Koch at a recent Board meeting of the operations the Committee would have called for thus far in 1964 if it had employed such a target. Perhaps there were answers to the questions raised by Mr. Koch's discussion, but he had not seen them. He was opposed to selecting a new target of this sort without a demonstration that it would involve a net gain for monetary policy.

The proposed element 4, Mr. Daane continued, would elevate free reserves to a status as an operating target even higher than that which the market believed, and some academicians had charged, that the Committee gave to it. He did not think the Committee should quantify its instructions and require the Desk to meet numerical targets, even if the instructions were tempered with qualifications. Moreover, he questioned the statement on page 7 of the memorandum that a change in the free reserve target would have "quick and significant" consequences for other policy variables. Mr. Daane doubted that the relations were such that quick and significant consequences would necessarily follow, or that the Committee knew precisely what the relations were at any time, even as between free reserves and bill rates. Thus, he would not subscribe to the use of free reserves in this manner, with the full weight of the Committee behind them.

Mr. Daane concluded by saying that he approached the proposal with two questions in mind: Would its adoption basically improve the Committee's performance, and would it improve the Committee's presentations to the public? Of the two questions, the former was by far the more important, and he did not see anything in the proposal that would improve the Committee's performance in the ultimate sense. Perhaps further analysis along the lines of elements 1 and 2 was desirable, but there was no need to incorporate it in the directive. He was puzzled by the implication on page 3 of the memorandum that variations in the rate of growth of bank reserves over a period when the Committee was voting for "no change in policy" were in themselves bad. "No change in policy" seemed to him to be a meaningful and significant conclusion that the Desk could and did interpret and implement.

Chairman Martin, noting the lateness of the hour, suggested that the meeting be adjourned at this point with the understanding that the discussion would be pursued at a later meeting of the Committee. Since there would be some absences at each of the next two meetings, he suggested that this subject be put down for further discussion at the meeting tentatively scheduled for September 29, 1964.

Chairman Martin said he knew that all of the Committee members appreciated the work Messrs. Ellis, Mitchell, and Swan had done in preparing their memorandum. He believed that it was important for the

Committee to continue to work on the problem of the directive. In this connection, the Chairman thought it would be useful if Mr. Hayes had copies of his comments today distributed to the Committee. He also thought the Committee might adopt Governor Robertson's suggestion that it make unofficial "trial runs" of a new type of directive, while continuing to employ its present type of directive officially. Accordingly, he suggested that for the next several meetings the staff prepare, on the side, the kinds of materials called for in the memorandum.

No objections were made to the Chairman's suggestions.

Thereupon the meeting adjourned.

Secretary