

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, September 10, 1957, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Hayes
Mr. Allen
Mr. Balderston
Mr. Leedy
Mr. Mills
Mr. Robertson
Mr. Szymczak
Mr. Vardaman
Mr. Williams
Mr. Irons, Alternate for Mr. Bryan

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

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

Mr. Riefler, Secretary
Mr. Sherman, Assistant Secretary
Mr. Hackley, General Counsel
Mr. Solomon, Assistant General Counsel
Mr. Thomas, Economist
Messrs. Marget, Mitchell, Tow, and Young,
Associate Economists
Mr. Rouse, Manager, System Open Market Account
Mr. Carpenter, Secretary, Board of Governors
Mr. Koch, Assistant Director, Division of
Research and Statistics, Board of Governors
Mr. Miller, Chief, Government Finance Section,
Division of Research and Statistics, Board
of Governors
Mr. Gaines, Manager, Securities Department,
Federal Reserve Bank of New York

Messrs. Abbott, Daane, Roosa, and Strothman,
Vice Presidents of the Federal Reserve
Banks of St. Louis, Richmond, New York,
and Minneapolis, respectively; Messrs.
Balles and Einzig, Assistant Vice Presi-
dents, Federal Reserve Banks of Cleveland

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and San Francisco, respectively; Mr. Walker, Economic Adviser, Federal Reserve Bank of Dallas; Mr. Anderson, Financial Economist, Federal Reserve Bank of Philadelphia

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the Federal Open Market Committee held on August 20, 1957, were approved.

Before this meeting there had been distributed to the members of the Committee a report prepared at the Federal Reserve Bank of New York covering open market operations during the period August 20 through September 4, 1957, and a supplementary report covering commitments executed September 5 through September 9, 1957. Copies of both reports have been placed in the files of the Federal Open Market Committee.

Mr. Rouse reported that he had been on vacation during a good part of the past three weeks, but so far as he could determine the money market had been consistently tight during this interval. Federal funds traded briefly below the discount rate the last two days of the September 4 statement week but remained at the ceiling rate during the rest of the period. The reserve projections beginning with the Labor Day holiday period consistently overestimated net borrowed reserves. Until the end of August, the projections indicated substantial tightness through the week ended September 11 and then two weeks of somewhat lower net borrowed reserves. On the basis of these projections, Treasury bills were purchased for the System account in the early part of the period. The currency outflow prior to the Labor Day holiday was

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smaller than expected, however, and float released more reserves than expected, with the result that the reserve figures had not been as tight during the past two weeks as anticipated, despite sales of Treasury bills from the System account. On top of all this, a substantial after-the-fact revision makes the net borrowed reserves figures look, in retrospect, even less tight than they did at the time the Desk was dealing with them. Mr. Rouse also commented that the sales from the System account in the past several days were made without a full go-around, in view of the pressures already present in the bill market.

Mr. Rouse pointed out that the projections attached to the supplementary report now indicate average net borrowed reserves somewhat above \$400 million for the week ending September 11 and significantly lower averages for the following two weeks, partly reflecting free reserves for a few days in the first half of the September 25 week. Although reserve positions were expected to ease further during the next two weeks in reflection of a large projected float bulge, Mr. Rouse felt that, in view of the Treasury financing, it was unlikely that much could be done to offset this release of reserves. The last week in the month, however, would call for supplying a large volume of reserves, assuming the continuation of current policy.

Mr. Rouse also mentioned Treasury plans to announce its new cash financing on Thursday, September 12, with books open Monday, September 16, and payment on Thursday, September 26. Market conditions

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suggest that the Treasury might find it easier to sell securities of more than one-year maturity than to sell shorter-term issues, he added, noting that a somewhat bullish atmosphere had developed in the bond market due to such influences as the lessened optimism on the business outlook, concern over the outlook for some foreign currencies, and testimony before the Byrd Committee that had been interpreted to suggest that interest rates may be near a peak. These changed expectations would help the market to absorb the large scheduled corporate and municipal offerings in the next few weeks as well as the proposed Treasury offering.

At the conclusion of Mr. Rouse's remarks, Mr. Balderston asked if the March 1958 tax bills were in supply or were being pressed on the market. Mr. Rouse replied that there were some March tax bills around but that they were not being pushed; evidently part of the issue that was loosely held had been distributed.

Upon motion duly made and seconded, and by unanimous vote, the open market transactions during the period August 20 through September 9, 1957, were approved, ratified, and confirmed.

At Chairman Martin's request, Mr. Young presented a report in which he compared the strong and soft spots of the economy at present with the situation of last spring. His statement was substantially as follows:

At the last meeting of the Committee, question was raised as to how the strong and soft spots of the economy

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now compare with the situation of last spring. In other words, what significant changes have occurred since last spring, and what do these changes indicate with respect to prospective near-term levels of activity? My report at this meeting will be directed to a capsule consideration of this broad question rather than to a specific summary of the staff memorandum circulated to you in advance.

The first and most obvious observation to be made about the economic situation is that activity, domestically and abroad, continues at high and fairly intensive levels of resource utilization. Reflecting strong and still expanding aggregate demand, wholesale prices are up somewhat from late spring and consumer prices are up sharply. Thus, price stability, for which there was some hope by late spring, has not yet been achieved, particularly at the consumer level.

Industrial production, which was showing modest downward drift during the spring, has since leveled out and is now possibly showing an uptilt. The current rate of steel production in relation to capacity holds higher than was expected last spring for this time of the year and the order flow is reported to be swelling again. Output of consumer goods has strengthened, with durable goods production, which had been declining during the first half of the year, showing revival. Average hours worked per week, seasonally adjusted, have generally shown some rise from spring hours, whereas hours worked in the spring had been declining for some months.

Construction activity has generally maintained record levels since the spring period, as it had earlier. For two years through the spring, residential construction activity had been declining and further decline over the balance of the year was rather widely expected. Since spring, residential construction activity has leveled out and then risen some. The building industry now expects further rise. If there has been any weakening in the construction area since spring, it has been in the industrial and commercial construction area, but the indications here are by no means clear.

Last spring, business plant and equipment expenditures were thought to be still rising, though at a much reduced rate. Still some further rise was expected, at least through the summer. Information now available points to a leveling out in the total of these outlays since the first quarter, with the near-term prospect for them to continue level.

New orders in durable manufacturing, which reflect adjustment in business plant and equipment expenditures as well as other influences, were declining last spring and had been for several months. Since June, they have been stable about 7 per cent under year-ago levels.

National security expenditures rose over the last fiscal year, and have risen further since. Recently cutbacks have been announced in defense outlay schedules and further sizable cutbacks will be required to bring defense outlays within budget estimate figures.

The immediate background of business inventory spending last spring was one of abrupt leveling off following two years of substantial buildup. This adjustment was in recognition of easier supply conditions and the large stocks in hand. With these conditions continuing, business inventory spending has since been held in close relationship with current sales, with only modest further growth in holdings.

Consumer spending for goods last spring also had an immediate background of leveling out. Consumer nondurable goods buying was showing some buoyancy, but purchasing of household durables was reduced, and buying of automobiles was running below industry expectations. With further rise in personal income since mid-spring, consumer buying of nondurable goods has picked up strikingly further, demand for household durables has shifted from softness to fair strength, and automobile demand, though supported by credit purchases more than any other year at this time, has held up much better than expected. Car buyers on credit during the 1954-55 new car sales bulge are becoming debt free in increasing numbers, and the automobile industry is looking forward to an active replacement demand from these car owners to support new model introductions this fall.

Foreign demand for U. S. goods as reflected in exports, though reduced from record levels reached earlier in the year, in consequence of lower petroleum shipments, appears from latest reports to be holding not too far below the high level reached in the first quarter.

Reflecting shifting supply-demand relationships in particular markets, price changes for basic industrial materials have remained selective. In nonferrous metals markets, weakness manifest in the spring and before has continued. In finished goods markets, recent price increases have probably been more numerous than in the spring, partly because of the recent increase in steel prices. They have not, however, been as widespread nor as large as in comparable months of last year. Prices of grain crops were weak in the spring and have weakened further since. Prices of meat

animals were strong in the spring and have strengthened further since.

Financially, aggregate credit and capital demands have continued to expand, and, with restriction on bank credit expansion, have intensified money and capital market pressures. Market interest rates since last spring have risen appreciably further--to a point, in fact, where they are pressing against levels prevailing in 1929. This development, together with uncertainties characteristic of the period of the year as well as special uncertainties arising at this time, has precipitated in recent weeks an abrupt re-evaluation of stock market yields and prices in comparison with those of alternative investments. Last spring rebound of business optimism, after an early-in-year wave of pessimism, was finding expression in rising stock prices and further declines in already low stock yields.

Last spring, business failures were at high postwar levels and the background for over a year had been one of steady rise. Similarly, new incorporations were low, and had a background of steady decline. Both of these series have shown positive reversal since spring.

Reflecting System policy, monetary expansion has been virtually absent since the spring. In early months of the year it had only been very modest. Another development since spring has been a slackening in the rise of money turnover. For banks, other financial institutions, and large business corporations, a still tighter liquidity position clearly obtains now than in the spring.

In Europe since spring, inflationary trends and foreign exchange market disequilibria have moved into a critical phase, with new or additional monetary restraints introduced in various countries and with further appreciable increase in market interest rates in all of them.

Although the money surface of the economy appears more disturbed than in the spring, the underlying economic situation does not differ enough from the spring to suggest prospects other than continuation of offsetting adjustments, at high levels of activity. Some inflationary symptoms persist but modest growth in total real output still appears to be a feature of the over-all developments. There is clearly no formation of forces indicative of imminent upsurge of general demand pressures. Neither does there appear to be present a combination of developments portentous of general downward adjustment. Should strength recently manifest in consumer markets be extended, strengthening of demand in semi-finished and primary material markets might

well be expected as a secondary response. With capacity in major material and manufacturing lines now well expanded-- and so temporarily a restraint on new business investment-- and with restrictive credit conditions continuing, the response of industrial suppliers to stronger demand might assume characteristics more overtly competitive in price terms than has been witnessed for some time. Such a development would signalize a breaking up of inflationary clouds.

There are competent business observers, especially in the financial community, who are inclined to the belief that major economic forces are shaping toward a downward drift ahead of general activity. These observers emphasize: (1) the cumulative inhibiting effects of monetary restraints on credit-financed investment; (2) a high and inflexible industrial cost structure; (3) a cumulating pressure of excess capacity on markets for industrial materials and fabricated commodities resulting from the swollen volume of business investment of recent years; (4) the prospect of a significant reduction in national defense expenditures during the current fiscal year; and (5) a developing psychology of gloom in high business places. This prognosis, which underlies some current pessimism in "informed financial circles," seems far out of focus in terms of the recently developing situation.

At the same time, as we have stressed before, one must recognize that, considering the complex of forces determining levels of economic activity, any prognosis of future prospects is dated. The economic situation must constantly be followed very closely, and assessments of it modified in the light of trends shown by newly available facts.

In response to a question from Mr. Vardaman as to when reductions in defense expenditures that were being discussed might become noticeable in their effects upon the economy, Mr. Young said that he felt the effects would appear almost at once. The real question, he said, was how much cutback actually would be effected, considering all of the circumstances; there was much talk of cutbacks, but up to the present time it had not been possible to obtain from either the Defense Department or the Bureau of the Budget any clear schedule of what they might be. For this reason it was not possible to evaluate at the present time

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their quantitative effects on economic activity.

Mr. Thomas next made a statement concerning recent credit developments as follows:

Principal developments in financial markets recently have been

(1) The continued large volume of payments by the Treasury.

(2) The continued large volume of new securities offered both by corporations and by State and local governments.

(3) The leveling out of bank credit expansion, reflecting a more moderate loan growth than in the two previous years and further liquidation of Government securities by banks.

(4) Some firming of the bond market at the high level of yields reached earlier, notwithstanding the large volume of new issues.

(5) The persistent decline in stock prices with light trading.

(6) The continuation of Treasury bill rates at slightly above the discount rates and the maintenance of yields on Government securities maturing in 6 months to 4 or 5 years at around 4 per cent.

(7) Continuation of member bank borrowing at a generally high level, even though at times less than was expected, with city banks showing tight reserve positions.

The continued high level of Treasury expenditures is disconcerting. General national security expenditures at an annual rate \$6 or \$7 billion above the budgeted figure for this fiscal year indicate that such spending has been an important expansionary force in the economy and also raise questions as to the future. The first question is whether the level can be effectively cut to within the budgetary limits and the second is what would be the effect on the economy of such a reduction. If the cut can be effected, it would release resources for other uses and help to relieve some inflationary pressures. If it should be accompanied by decreases in other lines of activity, the result might be a general decline in total activity, but the need for some reduction is the more serious and more immediate cause for concern. One question to which the answer is not known is to what extent the larger than expected expenditures reflect rising prices or an expanded program or to what extent a speed-up of program deliveries, which will be followed by a decline.

Large budget expenditures by the Treasury, together with continued substantial redemptions of savings bonds, are exerting a drain on the Treasury cash balance and necessitating frequent borrowing. The rate of spending must be reduced if the Treasury is to keep its borrowing within the statutory debt limit.

Business borrowing at city banks has increased less in the past five weeks than in the same period of other recent years--a little over \$300 million, on the basis of partial figures for the latest week, compared with close to \$600 million in 1956 and also in 1955. The increase since the end of May, including this year's large borrowing in June, has also been less than in the two previous years. Corporate borrowing in the capital market, however, has been very large, and some of these funds have gone into the payment of bank loans. It appears that in the aggregate business has received a substantial amount of credit. In addition to the very heavy volume of new issues being offered in September, the amount scheduled for October is also large.

Banks have tended to reduce their holdings of Government securities in recent weeks, notwithstanding important participation by banks in underwriting new Treasury cash-raising issues. Total loans and investments of city banks have shown little net change during the past three months.

Demand deposits adjusted, after increasing more than seasonally in June and July, have apparently shown a marked decline since the end of July. Little growth, on a seasonally adjusted basis, has occurred since last spring.

Bank reserve needs have conformed closely to the broad seasonal pattern in recent weeks. Net borrowed reserves averaged about \$470 million in August, compared with \$350 million in July. The country-wide average has been running less than \$400 million during the past week, with reserve demands over the Labor Day holiday being somewhat less than usual. Country banks have been able to reduce their borrowings and increase their excess reserves, but city banks currently are under a considerable amount of pressure with a rather large amount of borrowing and relatively small amounts of excess reserves.

The tight reserve situation at city banks and attempts by corporations and others to obtain cash for mid-September tax, dividend, and other payments have kept the bill market under considerable pressure during the last few days. This is a period when a high degree of liquidity is required in the money market. For this reason it may be difficult for the

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System to sell bills to prevent a further drop in net borrowed reserves in the next two weeks when float will be temporarily high.

On the basis of the usual seasonal pattern, early in October the System may need to purchase about \$300 million of securities, plus any amounts that may be sold in the next week, to keep net borrowed reserves close to the \$500 million level. Little additional Federal Reserve credit would be needed in November, but large amounts would be necessary in December. If a more than seasonal growth in the money supply should occur, demands for Reserve Bank credit will be larger than those projected. In that event a policy decision will need to be made as to how the additional reserves will be supplied--whether to require banks to borrow more from the Federal Reserve Banks, or to relieve the pressure through additional open market purchases. Current developments seem to call for neither a further tightening nor any relaxation of System policy.

Chairman Martin then called upon Mr. Hayes who commented on business activity and credit policy in substantially the following terms:

There has been no material change in over-all business activity since the last meeting, or, in fact, for the past several months. The economy is still characterized by stability of production and employment and by well-sustained consumer demand. On the other hand, there are no visible signs pointing to the strong upsurge in the fourth quarter which had been so widely expected early in the summer. Business sentiment, in contrast with current business statistics, has undergone a perceptible change in recent weeks in the direction of greater caution or even pessimism. Apparently this can be traced to (1) recognition of the growing gap between industrial capacity and actual output; (2) the fact that production has been maintained in the face of declining backlogs of unfilled orders and some accumulation of inventories at the manufacturing level; (3) prospective cuts in defense expenditures; and (4) increased concern over the position of various foreign currencies. The downward trend in stock prices may reflect similar influences and has in turn contributed to the changed climate of business opinion.

It seems unlikely that defense spending can actually be reduced rapidly and by substantial amounts. Hence the influence of this factor, if any, will probably continue to be mainly on business expectations rather than on visible statistics over the next several months. In the area of plant and equipment outlays, however, there is now a reasonably clear prospect for a decline in gross expenditures. The SEC estimates to be released shortly point to a small decline in the fourth quarter on a seasonally adjusted basis-- the first decrease since the current investment boom began. These figures are of course expressed in dollars. In terms of physical volume, the peak of investment in new plant facilities may already have been passed around the beginning of this year.

With supplies now ample in most lines, and with the public showing increasing signs of price consciousness, there seems to be hope at last of a leveling movement in prices in spite of the continued influence of some cost-push factors. Food prices, which have been largely responsible for the rise in consumer prices in the last month or two, have probably passed their seasonal peak. The weekly wholesale price index has been practically unchanged since mid-July.

Although bank credit has expanded somewhat less rapidly in the last four weeks than a year earlier, the banks continue to feel heavy pressure for loans, and the substantial reduction in bank liquidity since a year ago has intensified this pressure. For example, New York City banks are now estimated to have loans equal to 66 per cent of deposits as against 62 per cent a year earlier. Demands for funds in the capital markets continue at a very high level. The Treasury is expected to borrow about \$3 billion in a cash financing program due to be announced on Thursday, with the offering on September 16 and payment on September 26.

As for credit policy, it appears to me that the stability of the business situation points to the desirability of maintaining about the same degree of restraint as in recent months. If anything, the signs pointing toward possible weakening of the boom would suggest a slight relaxing rather than any intensification of restraint, but I think it would be confusing to the market to give any sign of relaxation so soon after the recent series of discount rate increases. It would be premature, too, to lessen the degree of real restraint just as we seem to have a fair chance of realizing the price stability which we have worked so hard to achieve by maintaining a vigorously restrictive policy through these recent months of sideways motion in the physical output of the economy. On the other

hand, we should certainly provide reserves without reluctance or delay as they are required to meet seasonal requirements later this autumn, as well as to enable the banks to underwrite the Treasury's prospective offering later this month. In so far as the next two weeks are concerned, the influence of float and return currency movements may make it necessary for the System Account to do some selling, but if current projections are borne out, sizable purchases will be called for in the week of October 2. It is perhaps worth noting that we are entering a period when normal seasonal pressures are likely to reinforce our policy of restraint. At such a time, as we noted in the autumn of 1956, a given level of net borrowed reserves may well mean a substantially tighter money market atmosphere than would be the case under other circumstances, and this should be doubly true this year after the substantial further loss of liquidity by banks and corporations in the past year. Thus I think it would be well for the Manager to have ample leeway to maintain an even keel without being tied too closely to any target figure for net borrowed reserves. And while \$400 to \$500 million of net borrowed reserves was considered a reasonable range at the last meeting, it might turn out that the same degree of real tightness could be achieved in the coming weeks with a somewhat lower figure.

Mr. Johns said that he had come to this meeting prepared to take the position already suggested in Mr. Thomas' concluding remarks and reinforced by Mr. Hayes in his comments, namely, that for the time being no intensification of credit restraint was indicated and there was not yet an indication for relaxation. However, there seemed to be developing in the group with which he regularly discussed open market matters at the St. Louis Bank a view--as yet a somewhat minority view--that the time for some relaxation of monetary restraint might be imminent. Mr. Johns said that he could not accept that view at this time and therefore for the immediate future would keep the

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situation about as it has been recently. There was evidence that banks were under pressure in many places, he noted, but that was not true in St. Louis. However, banks in Memphis were under pressure because of the necessity for financing considerable cotton a few weeks ago, and in recent days Louisville banks appeared to have been under considerable pressure and were heavy borrowers.

Mr. Williams said that in the Third District over-all business was at a high level. Sentiment was not as good as the statistics and there were some soft spots, with businessmen somewhat less optimistic as to prospects for the remainder of the year. Total consumer buying was holding up fairly well. There were reports of pressure on manufacturers of hard goods and some of them who had lost dealer accounts had established distribution outlets of their own. Mr. Williams repeated that the views of business leaders on the whole were less optimistic than a few weeks ago. The outlook for the steel industry showed little change recently; textile operations were slow but the decline that had been noted for some time seemed to be leveling out. Smaller manufacturers felt that the real squeeze was on in terms of profits.

With respect to banking, Mr. Williams reported that loan demands at Third District reporting member banks in August were somewhat less than nationally and total loans of district banks declined. Deposits also were off somewhat. Borrowings by member banks continued

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at a high level although there had been some significant shifts in the sources from which the banks were obtaining funds in connection with changes in the discount rates and rates on Federal funds during August. Mr. Williams stated that he would suggest no changes in the Committee's policy at this time.

Mr. Fulton described activity in the Cleveland District as continuing at a high rate. The pickup in the steel industry had not been as great as had been hoped, partly because of the later model changeover for the automobile industry this year than in 1956. Also, the automobile industry seemed to be shortening its projections for steel needs as compared with last year, waiting to see how the new model automobiles would sell before placing orders ahead. Softening in the demand for oil goods and plumbing equipment had occurred, and appliance manufacturers had reduced their takings of sheet steel and also scheduled lay-offs recently. The railroad industry was taking large amounts of steel. Businessmen by and large seemed optimistic that a pickup would occur later in the year. The machine tool industry was shipping more than it was receiving in new orders, but this was not considered undesirable since it helped the industry to improve its delivery schedule. Mr. Fulton reported that, contrary to a statement of a New York banker reported by Mr. Thomas, there was some demand for term loans in the Cleveland District where firms preferred to obtain credit through that source rather than to go into

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the capital markets. There had been a slight contraseasonal decline in employment. Price changes were continuing with roller bearings, aluminum, and rubber showing increases.

Mr. Fulton stated that his conclusion was that the same degree of restraint on credit expansion that had existed should be continued for the time being. There should be no relaxation. He felt that any gradual relaxation would be a mistake; if it became necessary to change policy, it would be preferable to do it in a way that would have a positive impact. He suggested a continuation of the present degree of restraint and of the present policy directive of the Committee.

Mr. Robertson said that he was somewhat disturbed in reading the staff economic report prepared for this meeting, showing that net borrowed reserves had averaged under \$400 million since the meeting of the Committee on August 20. This confirmed the feeling of disquietude that he had had over recent weeks in reading the daily reports on the market situation that are obtained from the desk. He then went on to make a statement substantially as follows:

My concern about recent reserve developments stems from two reasons: first, I agree wholeheartedly with Mr. Young's statement this morning that the current business and economic situation remains strong; secondly, I feel that the net borrowed reserve figure, despite its shortcomings, is still our best indicator of over-all credit and money market conditions.

The task of the Manager of the Account is to carry out the will of the majority of the Open Market Committee, even though he may think that the minority point of view is more sound. And yet, it seems to me that the account has not only been aiming at the very bottom, if not below, the broad range of net borrowed reserves desired by the majority at our last

meeting, but that it has also been reluctant to take offsetting action when the actual net borrowed reserve figures have continued to be below those projected.

I have this feeling even though I recognize, first, that in view of continuing Treasury financing problems the account was given a wide range of latitude at our last meeting, and second, that part of the difference between actual and projected net borrowed reserves in recent weeks has been due to unforeseeable changes and revisions in certain factors affecting reserves. Nevertheless, I continue to be struck by the inactivity of the account when net borrowed reserves fall below the general target range in contrast to the rapid corrective action generally taken when these reserves go above the target.

Turning from the past to the future, assuming there was some justification for the view that when short-term interest rates were rising rapidly, as they were a few weeks ago, a somewhat lower level of net borrowed reserves than our target of from \$500 to \$600 million was consistent with the maintenance of the prescribed degree of restraint; now that the rise in interest rates has slackened somewhat, a level of net borrowed reserves of under \$400 million is not sufficiently restrictive.

The delayed and inadequate action of the desk in offsetting decreases in the average level of net borrowed reserves since the last meeting of this Committee is particularly troublesome because of the imminence of another Treasury cash financing and the temporary further drop in net borrowed reserves that will occur in the weeks immediately ahead as the result mainly of the usual mid-monthly increase in float. Therefore, I would strongly urge that the Manager of the Account do all that he can, both before and after the announcement of the financing, to keep net borrowed reserves within the range prescribed.

Mr. Rouse stated that it was quite clear to him at the August 20 meeting that the majority of the Committee was aiming at net borrowed reserves in the \$500-\$600 million range, whereas the operations had turned out to be closer to the \$400-\$500 million range. This was the result of the developments that had taken place in the market and in no way reflected bad faith in attempting to carry out the Committee's directive.

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Mr. Mills stated that, granting that intuition was an unreliable guide, his intuition told him that Labor Day marked not only a seasonal turning point but also a turning point in movement of economic activity that deserved the Committee's attention. With the change to a decidedly more pessimistic attitude on the part of the business community, he believed that the strain of conservatism that had developed, along with the reduced corporate and commercial bank liquidity that was so much in evidence, could in a very real way take over some of the System's responsibilities for exerting restraint over general economic activity. On that assumption, it would be logical for the Committee not to aim at too high a target level of negative free reserves, Mr. Mills said, and a level of around \$400 million should be adequate to carry out the System's policy of general credit restraint on commercial bank credit expansion. Along that line, he noted a movement of the supply of reserves out of the central reserve bank cities and to a lesser extent out of reserve city bank cities to country areas as harvests are completed. The proceeds of harvests had lodged in banks in these country areas and, having lodged there, did not move with readiness back into the money market areas. That being the case, where the total supply of reserves might seem abundant, there could still be a starving of reserves at the city bank levels. Consequently, Mr. Mills felt that allowing some reserve leniency at the central reserve city bank level

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should not touch off an undesirable expansion of bank credit. Therefore, his thinking had brought him to the conclusion that for the present the System could accept a lower level of negative free reserves without losing the tangible degree of credit restraint that is essential to the maintenance of economic stability. The great question in his mind was whether the credit resources and economic factors that might be disengaged from the capital expansion program would move through the process of a rolling readjustment to employment in other areas, such as housing, in a manner that would maintain a stable, high level of economic activity.

Mr. Vardaman complimented Messrs. Young and Thomas for the clear and comprehensive reports they had presented to the Committee this morning on the economic and credit situation. His view was that the Committee should make no change in its policy or in the general operations to carry out that policy during the next three-week period. He agreed with the suggestion by Mr. Hayes that the trading desk should have considerable leeway in its operations pursuant to the Committee's policy directive. Mr. Vardaman emphasized, however, that he felt transactions for the System Open Market Account always should be confined to the shortest maturity Treasury bills.

Mr. Leach reported that the Fifth District economy was displaying no strong tendency toward change in either direction. The principal industries were continuing at their summer pace. Bituminous

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coal production was still expected to exceed 1956 although by a smaller margin than was earlier thought. Coal loadings through Hampton Roads and Baltimore ports in early August were 13 per cent ahead of last year but were expected to decline in the coming months. In response to a later question by Mr. Vardaman, Mr. Leach said that a substantial part of coal shipped from Fifth District ports was destined for Western Europe.

With reference to the textile industry, Mr. Leach said that the long expected upturn was still awaited. Despite cutbacks to 4- and 5-day weeks in most mills, production was still in line with sales. Defense Department cutbacks in the number of civilian employees had been announced, he noted, but they did not bulk large relative to total employment of that type in the Fifth District. There were scattered reports of declines in employment by Government contractors whose contracts had been curtailed. More than offsetting these cutbacks was the recent award to the Newport News Shipbuilding and Dry Dock Company of the construction of what was expected to be the largest ship ever built, namely, a \$311 million atomic-powered carrier. Recent rains had helped Fifth District crops, but good tobacco prices were only a slight offset to the smaller crop grown on the curtailed acreage.

In so far as the national economy was concerned, Mr. Leach said that he saw no significant shift in either direction although he did sense some change in expectations for the rest of this year.

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There now seemed to be no boom psychology, and fewer people expected a sizeable upsurge in business this fall. On the other hand, retail prices were still increasing and expectations of continued increases over the long run did not seem to have diminished. Mr. Leach commented on a Washington newsletter which predicted that prices would be 15 per cent higher in 10 years and 50 per cent higher in 25 years and which recommended certain hedges against inflation. While coming weeks might show some delayed effects of the System's past actions toward restraining credit expansion, for the time being he would oppose any relaxation in the policy of credit restraint. He felt that the Committee should aim at the same degree of tightness that had been its objective recently, and he suggested that as a benchmark the objective might be for net borrowed reserves of around \$450 million during the next three weeks.

Mr. Leedy said that although he had been away from the Tenth District during most of the period since the August 20 meeting, the statistics indicated no material change in district conditions during that period. Some increase in business loans was occurring a little later this year than was ordinarily the case, presumably because of the later harvest. Mr. Leedy referred to the comment Mr. Hayes had made as to the loan-deposit ratio of New York banks, stating that in contrast with the New York ratio of around 66 per cent, Tenth District banks now had loans equal approximately to 43 per cent of their deposits-- only slightly higher than a year ago.

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Mr. Leedy felt that the general picture required a continuation of the policy the Committee had been following and said he would subscribe to the view that for the next three weeks we should attempt to apply the degree of restraint that had been aimed for during the preceding three weeks. Like Governor Robertson, he had observed that the target of net borrowed reserves had been missed during this period, as he had understood the discussion at the August 20 meeting, but he was under the impression that this was the result of the difficulties in making accurate projections of factors that influenced reserves. In any case, he could see no reason for a change now in the course the Committee had been following.

Mr. Allen concurred in Mr. Vardaman's comment on the reports of Messrs. Young and Thomas. He went on to say that he had observed growing signs of uneasiness in business sentiment during the past month, following the shifts of the past year from optimism to pessimism and back again. He found it hard to rationalize the recent tendency toward uneasiness with actual developments. Perhaps the best explanation was there had been a sobering recognition on the part of the business community that a great deal of the good business of the past few years had been financed by borrowing and that presently indebtedness was heavy in almost every sector of the economy. Mr. Allen felt that this situation might at last be affecting business sentiment. Recent developments otherwise could not be called depressing.

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Mr. Allen recalled that at the preceding meeting he had mentioned the renewed uptrend in retail sales. Since then, figures on sales at department stores had been well maintained both in the Seventh District and in the nation as a whole. Sears, Roebuck and Company had reported that August was one of the best months the company had ever had. The whole picture indicated that consumers had increased their buying this year in line with the 6 per cent rise in their incomes. The current caution on the part of businessmen might reflect the difficulty in employing profitably the enlarged productive facilities which had been constructed with the help of large sums of borrowed money.

Mr. Allen then reported on the agricultural situation, noting that prices received by farmers in mid-August averaged 5 per cent above the year-earlier level. Meat animals had led the advance, while feed grain prices were substantially lower than last year. That situation should result in increased production of meat animals.

With respect to the automobile industry, Mr. Allen said that he had obtained information from Detroit yesterday that inventories of new finished automobiles totaled 832,000 units on September 1, including 20,000 of the new Edsels. The figure of 812,000 of 1957 models was high, but in the last ten days of August sales averaged over 20,000 units a day, and if this rate were continued it would help reduce the stocks substantially. The industry was generally optimistic on prospects for

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cleaning up current year models. Output of new cars for the fourth quarter of this year was expected to total 1,600,000 units--the same as in the final quarter of 1956.

Turning to bank credit, Mr. Allen said that business loans at reporting Seventh District banks increased only \$3 million in August this year compared with \$43 million a year ago. Demand for loans may be less, but Mr. Allen felt that banker resistance to increasing loans was the more important factor. He noted reports from bankers that the proceeds of new security issues were being used in many cases to repay bank loans. Mr. Allen then presented the results of a survey on the mortgage situation made in the Seventh District during the past week. It did not appear, he said, that recent changes in FHA terms were proving to be a stimulus to mortgage lending, although a month's experience coming at a time when building activity was beginning to taper off could not be considered as conclusive. Since the new FHA rates permitting a total charge to the borrower of 5-3/4 per cent went into effect on August 6, there had been a further tightening in the availability of mortgage money. The net return on FHA-insured loans (allowing for a discount of 2 points) would provide a yield of about 4.95 per cent on a 25-year loan, which Mr. Allen felt was not quite enough to make such loans attractive in comparison with yields on some of the recent high grade bond issues. Furthermore, lending had been highly selective and some of the institutional lenders had

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refused to go along on the lower FHA down payments. Mr. Allen also said that any change in the flow of new corporate issues could alter this mortgage situation markedly, particularly since there was some evidence that cash reserves were being accumulated which could be put to work quickly if it became apparent that the rise in interest rates was reaching a crest. Another factor influencing the situation was the upward movement in rates being paid on savings. Savings and loan associations were paying 3-1/2 to 4 per cent and they apparently needed a 2 per cent spread between those rates and the yields on new investments.

As to monetary policy, Mr. Allen said he believed the Committee should continue the degree of restraint it had sought recently as far as that was possible. He referred to Mr. Rouse's earlier comment that the desk would try to sell Treasury bills during the next few days and stated that he did not know what more it could do. The Committee talked about giving the desk leeway, Mr. Allen said, and of course the desk must have leeway. He believed, however, that the desk had tended to recognize that leeway more on the down side than on the up side, and he thought there were times when it could lean in the direction of having larger rather than smaller net borrowed reserves than the targets indicated by the Committee.

Mr. Deming said that activity in the Ninth District seemed to be picking up a little with the gain somewhat more than would be

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expected seasonally. Expectations for the fourth quarter were for a continuation of this kind of record, that is, for something a shade better than the regular seasonal rise. Employment in nonagricultural lines was stronger, and retail sales continued good. Iron mining activity was high, but nonferrous mining continued weak as did lumber production. The farm picture continued good with income rising. Livestock producers had had the best year in 1957 since 1951; ranges and pastures had been good all season and winter feed supplies would be ample. Business loans in the Ninth District had dropped slightly in the past three weeks and total loan growth had moderated; deposit growth also had been less than in the comparable period of last year. All of this added up to a picture of no strong rise in credit or in the economic situation in the forthcoming period, Mr. Deming said, and although there was no sign of any great weakness, his conclusion was that the Committee's present policy should be renewed, aiming at substantially the same degree of restraint that had been had during the past three weeks.

Mr. Mangels said that the Twelfth District economy had not shown much change in recent weeks. Nonferrous metals mining had been curtailed with some of the smaller operations having shut down and others having shortened their workweek. Aluminum production in the Pacific Northwest would be reduced in September because of the power shortage and some permanent shutdown might result in aluminum production because of the power problem. The lumber industry was still feeling a pinch.

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Department store and automobile sales were holding about even, but department store managers were hard put to maintain sales volume at the existing level and were using special sales and other devices. Steel output in the Twelfth District area declined from 97 per cent of capacity in June to 91 per cent in July. Loans of reporting member banks in the Twelfth District during the four weeks ending August 28 increased \$49 million, Mr. Mangels stated, the same as in the corresponding period of 1956. Commercial and industrial loans and consumer loans had increased, while real estate and agricultural loans declined during this period. Demand deposits declined during recent weeks while savings deposits continued to increase. Borrowings of Twelfth District banks continued moderate.

Mr. Mangels stated that the over-all situation as a whole continued somewhat mixed with no definite trend either up or down. The economy is not experiencing over-all pressures of demand in relation to productive capacity that might force prices up further, and it has virtually no unemployment. Until a tendency in one direction or the other is more clearly discernible he would suggest no change in the Committee's directive or in the general program of credit restraint, and during the next three weeks would aim for net borrowed reserves at about the \$400 million level. He would not be inclined to aim at a figure as high as \$500 million.

Not much change had taken place recently in the Dallas District situation, Mr. Irons said. The petroleum situation continued about as

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he had reported it at recent meetings. The agricultural situation was favorable with good grain crops, a good outlook for cotton production, and favorable livestock prices. Agriculture was in the best position that it had been in for several years. Retail trade was holding well and employment was at record levels. Construction declined in August. Automobile sales continued fairly good and for the year to date were about 10 per cent ahead of a year ago. Selling activity was intensive, Mr. Irons said, but there was not much sign of price cutting. Bank loans had increased moderately during recent weeks, compared with a slight decline a year ago. Bankers with whom he had talked recently reported that loan demand continued very strong and that this included considerable demand for term loans. Member banks were borrowing from the Dallas Reserve Bank more than they had been a short time ago, with discounts in the \$28-\$35 million range, compared with a \$15-\$18 million range prior to ten days ago. Borrowings were mostly by reserve city banks where the reserve position had been negative, while country banks were continuing to have reserves around 10 per cent in excess of requirements.

With respect to the "pessimism" reported among businessmen, Mr. Irons said that he could see nothing in the Dallas District that could be considered as pessimistic. Bankers were more cautious than they had been a few months ago but he had not found pessimism. The factors that perhaps justified this feeling of caution included: (1) an

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assumption that the Federal Reserve would continue to maintain a policy of firm restraint and for this reason bankers generally could see little chance of a breakthrough on the up side, and (2) bankers were anticipating and were hoping that there might be a substantial cutback in Federal Government expenditures--this feeling having developed as a result of press comments emanating from Washington in recent months.

As far as credit policy for the next three weeks was concerned, Mr. Irons said that he would like to have the Committee maintain a policy of firm restraint. There was greater risk that the Committee might ease off too soon rather than maintain firm restraint too long, he felt. While he did not place much reliance on any figure of net borrowed reserves, if he were to name one he would prefer something in the neighborhood of \$500 million. He would expect that discounts would continue around a billion dollars. He would hope that the short-term rate would move around the discount rate. Mr. Irons said that he would generally prefer to be on the side of firm restraint over the next three-week period, to wait before moving on the side of easing, and to resolve doubts on the side of restraint.

Mr. Erickson stated that no significant changes had occurred in the First District economic situation in recent weeks. Business sentiment was considerably more cautious than it had been earlier. Nonfarm employment during July was higher than in June. Shoe production for the first seven months of 1957 was down 3.5 per cent from a

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year ago, but 1956 had been an excellent year. The newspaper strike in Boston had affected department store sales unfavorably, but now it was over some signs of pickup were being observed. Construction contract awards turned up in July and were ahead of July a year ago. Mutual savings bank deposits in the First District were still increasing but at a slower pace than they had been earlier. Rates being paid on savings deposits were tending higher. The discount window at the Boston Reserve Bank was being used less actively than it had been earlier. The loan deposit ratios of Boston banks were fairly high, as had been indicated by Mr. Hayes for New York banks. Mr. Erickson expressed the view that this was partly the result of a decline in deposits rather than an expansion in their loans. As to Committee policy, Mr. Erickson said that he would continue the same firm restraint during the next three weeks that had been followed in recent weeks, neither intensifying nor relaxing during this period.

Mr. Szymczak said that while he was not as certain as Mr. Mills seemed to be that there had been a change in the economic situation, he believed that the Committee should lean in the direction of a \$400-\$500 million range in net borrowed reserves during the next three weeks. This was especially true because of developing seasonal needs and because of the Treasury financing that would be needed during the remainder of this year. Mr. Szymczak felt that it was necessary to be cautious in administering monetary policy, recognizing that many of the problems were more difficult when it came to carrying out operations than they

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appeared to be in discussions at meetings of the Committee. Different factors came in to affect the tone of the market. In a period of reduced negative free reserves, there might well be other factors in the picture that would result in a tighter situation than the figures of reserves indicated. For this reason, Mr. Szymczak said that he would give the Manager of the System Account as much leeway as possible in carrying out operations pursuant to the Committee's general policy, with the general thought that it would be desirable to aim at a degree of restraint that would be indicated by net borrowed reserves around \$400 million.

Mr. Balderston noted that we had heard conflicting testimony that the rolling adjustment still continued to roll and that loan demand was accelerating at a lesser pace than was true a year ago, even though part of the explanation was that borrowers had tapped the capital markets in order to obtain money to pay off bank loans. His concern about this situation stemmed from his inability to discern how much impact the cutbacks in defense expenditures might have on the economy. He recalled Mr. Thomas' observation that in the spring of 1953 the business decline came from cutbacks in defense expenditures of perhaps \$12 billion.

Whatever the reasons, it appears that current defense expenditures have gotten out of hand and that to get back to the level budgeted will require a drastic reduction. As part of such a cutback, the Defense Department might restrict its advance payments to contractors

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and thus throw a greater loan demand on the commercial banks.

In general, Mr. Balderston said that the fall outlook seemed to him to be good. He would suggest net borrowed reserves in the \$400-\$500 million range during the next several weeks, realizing that the trading desk might have difficulty in getting above the \$400 million level during the next two weeks.

Mr. Balderston then brought up the question how the desk would take care of dealer needs during the substantial forthcoming Treasury financing and at the same time work toward getting net borrowed reserves into the range indicated at this meeting. He referred to a comment by a Government securities dealer to the effect that sometimes dealers were able to get repurchase agreements easily while at other times they were made available by the System account only with reluctance. The dealer also observed that in some cases it took only a few minutes to know whether repurchase agreements were available, whereas in other cases such information could not be obtained for perhaps three hours.

Mr. Rouse said that he did not anticipate a need for repurchase agreements during this Treasury financing. Funds should be ample throughout the period, and he did not contemplate making repurchase agreements available. With respect to letting dealers know when repurchase agreements would be used, Mr. Rouse commented that it was customary to indicate by noon or shortly after whether the System account wished to make funds available on any given day through this means. This gave dealers time to scout around the country during the

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morning hours to find out whether funds were available elsewhere, and it was usually noon or a little later before the desk had a real indication of the pressure that existed. Dealers would, of course, be glad to be assured at the beginning of the day that funds were available at the repurchase rate, and, in some instances, when the account knew at the beginning of the day that it would wish to put funds into the market through repurchase agreements, a suggestion that repurchase agreements would be available might be given to the dealers in initial daily contacts. However, Mr. Rouse pointed out that making funds available in this manner was at the initiative of the System and that a procedure which gave the dealers the initiative would mean that the System account would have to take offsetting action at times.

At the conclusion of a discussion of the question raised by Mr. Balderston, Mr. Rouse said that he had discussed the general use of repurchase agreements with dealers along the foregoing lines and that he believed there was a fairly good understanding of the procedure followed by the trading desk and of the reasons for that procedure.

Chairman Martin stated that it seemed clear that the consensus at today's meeting was that there should be no change in the Committee's policy and no change in the wording of the directive at this time. He noted that most of the discussion at meetings of the Committee since early July had been about execution of Committee policy rather than about policy itself. Chairman Martin said that on returning from a brief vacation, he sensed a feeling of real encouragement as to the progress

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the System was making. He also was encouraged with the discussions that had been taking place in these meetings: all who were participating were learning a great deal and getting a better grasp of the problems the Federal Reserve was dealing with. He could not help but be conscious of the load that the Committee placed on the Manager of the System Account, he said, noting that the Committee issued a directive and then expected the Manager to keep in mind the majority and minority views expressed.

After stating that he had no real idea whether business was going up or down at the moment, the Chairman commented that he had been fishing during the past few days and that the thought had occurred to him that "the System has the fish on the hook." Its policy of restraint is now understood from one end of the country to the other. However, it would be a mistake for the System to hold so tightly on the hook that the line would snap, and this could happen if the tightness were so great as to embarrass the Treasury seriously. Chairman Martin said he did not think the Committee should minimize the difficulties that were facing the Treasury. This had nothing to do with a change in general policy, he noted, but it did involve a problem for the Manager of the System Account who had to carry on operations on the basis of tone, color, and feel of the market. The Chairman would align himself with the views expressed that there should be no change in policy at the present time, but it was always necessary to resolve doubts one way or the other in carrying out Committee policy, and for

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the immediate future he would resolve these doubts on the side of ease rather than tightness. He felt that the Committee's directive gave the Manager of the Account a clear indication of its policy but this did not mean that there would be any inconsistency if some "minor ease" were permitted during the period of the Treasury's financing.

Chairman Martin noted that some of the comments at this meeting had referred to a net borrowed reserves target of \$400 million while others had suggested \$500 million. He thought these differences were not significant, but he said that it would be undesirable if the market were to become "sloppy." Also, it would be a serious mistake if the business community were to get the feeling that the Committee's policy had been changed away from a policy of restraint to one of ease-- something that clearly was not contemplated.

The Chairman went on to say that he did not think the problem of inflation had been licked and he doubted that this would occur until there had been a modest correction of past excesses. He did not know when such a correction would come, but there had been many excesses in the course of the past eighteen months and adjustments would have to be made at some point. When that time arrived, he doubted that the Federal Reserve would have enough curative powers to arrest the type of decline that might occur, although it could contribute to psychological aspects of the situation.

As far as the present was concerned, Chairman Martin felt there had been a distinct gain on the psychological front. This was reflected

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in the stock market and by Mr. Irons' comment that bankers were cautious partly because they now felt that the Federal Reserve would maintain a firm policy of restraint, a view that was not widespread four months ago but which was widely accepted now. He also referred to Mr. Robertson's comment that despite their weaknesses, the net borrowed reserve figures were the best guide to operations for the System account. Chairman Martin stated that he still considered the limitations of the net borrowed reserve figures to be too great to make them of use as more than a target. The Committee may have set the wrong target at times, although this was a matter of judgment. The Treasury has a particularly difficult problem at this juncture, he noted, and its problems might have been compounded by the swings in net borrowed reserves.

In concluding his remarks, the Chairman said that he believed the fish was hooked and that it would be a mistake to pull the line so taut that it might break. He would cast his lot on the side of net borrowed reserves of around \$400 million, using that as a rough target, rather than the \$500-\$600 million range, until after the current Treasury financing was out of the way. He did not think such a procedure would cause any comment about a change in the System policy.

Chairman Martin then inquired whether there was any disagreement with the general policy aims he had stated or whether there were any suggestions for change in the Committee's directive.

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Mr. Allen said that he did not see how the Manager of the System Account could hope to attain a figure of \$400 million of net borrowed reserves over the period of the next two weeks unless there were unexpected developments; he felt that the Committee should recognize this in giving its instructions today.

Mr. Rouse stated that he too recognized the difficulty of attaining a \$400 million net borrowed reserve figure in this period. He also reviewed the figures for the past three weeks, stating that he felt that Mr. Robertson's earlier comments had indicated a greater departure from the Committee's target than was actually the case.

Mr. Hayes said that he felt the point Mr. Allen had made as to the difficulty of getting net borrowed reserves up to the \$400 million level during the next two weeks was important. The projections indicated figures of \$100 to \$200 million during some of this period, and it was probable that actual net borrowed reserves would fall short of the target that had been discussed.

Mr. Allen said that he also wished to give some support to the thoughts Mr. Robertson had expressed that the trading desk seemed more inclined to resolve doubts toward the minimum of the net borrowed reserve target rather than toward the maximum. He had been on the wire during the morning telephone call the past three weeks and early in that period the System account had purchased acceptances when the demand was so strong that the rate was lowered. At times of such

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strong demand, he said, the System might save its ammunition.

Chairman Martin stated that it was important that these matters be discussed freely and fully at any meeting of the Committee. He wanted Mr. Rouse to feel free to bring up questions or comments as to the operations of the trading desk.

Mr. Rouse stated that he would like to bring up a question concerning the rate on repurchase agreements. If repurchase agreements should be needed in the next three weeks, he had in mind the desirability of increasing this rate from 3-1/2 per cent to 3-5/8 per cent in order to break the connection between the discount rate and the rate on repurchase agreements so as to avoid the kind of box the System found itself in prior to the most recent discount rate increase. At that time, the rate on Federal Reserve repurchase agreements was so attractive when compared with rates on any other financing that dealers naturally were tempted to turn to the Reserve Bank first. At the same time, Mr. Rouse said he had hesitated to increase the repurchase rate since such action might have been viewed as a signal that the discount rate would soon be increased. A 3-5/8 per cent rate would still be attractive in comparison with current yields on short-term Governments, and would be in line with rates dealers are paying to finance. In response to a question from Mr. Mills as to whether such an increase would discriminate against nonbank dealers in Government securities, Mr. Rouse indicated that he did not think this would be the case, noting that banks operating dealer departments do not

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borrow specifically to finance that department and, in any event, bank access to the discount window had been somewhat limited under the discount policy currently being followed. Mr. Rouse emphasized that he did not anticipate using repurchase agreements before the next meeting of the Committee, although there might be some use toward the end of the period and it might then be desirable to make the change in rate suggested. During a brief discussion of this question Chairman Martin suggested that, if Mr. Rouse anticipated a change in the rate, it might be desirable to have an informal telephone discussion of the matter before such a change was made, and it was understood that Mr. Rouse would bring up the question on the morning call the day before he contemplated changing the rate.

Thereupon, upon motion duly made and seconded, the Committee voted unanimously to direct the Federal Reserve Bank of New York until otherwise directed by the Committee:

(1) To make such purchases, sales, or exchanges (including replacement of maturing securities, and allowing maturities to run off without replacement) for the System open market account in the open market or, in the case of maturing securities, by direct exchange with the Treasury, as may be necessary in the light of current and prospective economic conditions and the general credit situation of the country, with a view (a) to relating the supply of funds in the market to the needs of commerce and business, (b) to restraining inflationary developments in the interest of sustainable economic growth while recognizing uncertainties in the business outlook, the financial markets, and the international situation, and (c) to the practical administration of the account; provided that the aggregate amount of securities held in the System account (including commitments for the purchase or sale of securities for the account)

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at the close of this date, other than special short-term certificates of indebtedness purchased from time to time for the temporary accommodation of the Treasury, shall not be increased or decreased by more than \$1 billion;

(2) To purchase direct from the Treasury for the account of the Federal Reserve Bank of New York (with discretion, in cases where it seems desirable, to issue participations to one or more Federal Reserve Banks) such amounts of special short-term certificates of indebtedness as may be necessary from time to time for the temporary accommodation of the Treasury; provided that the total amount of such certificates held at any one time by the Federal Reserve Banks shall not exceed in the aggregate \$500 million;

(3) To sell direct to the Treasury from the System account for gold certificates such amounts of Treasury securities maturing within one year as may be necessary from time to time for the accommodation of the Treasury; provided that the total amount of such securities so sold shall not exceed in the aggregate \$500 million face amount, and such sales shall be made as nearly as may be practicable at the prices currently quoted in the open market.

Chairman Martin referred to a letter addressed to him under date of August 21, 1957 by the Honorable Wright Patman regarding the requests he had made in his letters of August 14, that information concerning policies of the Federal Open Market Committee and operations of the System Open Market Account be furnished to the House Banking and Currency Committee for the use of himself and other members of the Committee. The earlier requests had been discussed at the meeting on August 20 at which time the Committee gave a blanket authorization for the furnishing of such noncurrent information as appeared feasible and proper in response to this and other requests of Mr. Patman. In taking that action, it was understood that Messrs. Riefler and Rouse would

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confer with respect to preparing and furnishing the information requested in Mr. Patman's letters and in a list of questions dated August 6, 1957 submitted to Chairman Martin at the hearings before the House Banking and Currency Committee on the Financial Institutions Act.

At Chairman Martin's request, Mr. Riefler commented on a draft of reply to Mr. Patman's letter of August 21, copies of which had been distributed before this meeting. Mr. Leedy suggested a change in the second paragraph; Mr. Allen had not had an opportunity to read the letter carefully but it was understood he would do so and give Mr. Riefler any suggestions he might have.

The letter as changed was approved unanimously, subject to further suggestions from Mr. Allen.

Secretary's note: Mr. Allen having informed Mr. Riefler that he had no suggestions for change, the letter, prepared for Chairman Martin's signature, was sent to Mr. Patman later in the day in the following form:

"This letter is in response to your letter of August 21, 1957, in so far as it relates to furnishing of information to the House Banking and Currency Committee regarding operations of the System Open Market Account.

"Because some of the open market information requested in your two letters of August 14, 1957 has not been published, your requests were taken up at the meeting of the Federal Open Market Committee held on August 20, 1957, in accordance with the provisions of the Committee's Rules on Organization and Information regarding disclosure of unpublished information. The Committee authorized the furnishing of all information requested that could be supplied without disclosing policy decisions governing recent or current operations. In accordance with this view, the Committee felt that it would not be

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"proper to divulge at this time information regarding Committee policy decisions and operations relating thereto for the current calendar year.

"Information regarding individual sales, purchases, and repurchase agreements made pursuant to instructions of the Federal Open Market Committee from the date of the Treasury-Federal Reserve Accord, March 4, 1951, to the end of 1956 is being compiled. Preparation of this information involves a substantial amount of work, including the photostating of approximately 1700 pages of records, but it appears that the material will be ready before the end of this month.

"One of your requests was for a copy of each instruction or policy guide issued by the Open Market Committee to the Manager and to the Secretary of the Open Market Account. The Committee issues its policy instructions or guides for transactions in the open market to the Federal Reserve Bank of New York, which is the Federal Reserve Bank selected by the Committee to execute transactions for the System open market account; such instructions are not addressed to the Secretary of the Committee or to the Manager of the System Account. All policy instructions are made a matter of public record in the Record of Policy Actions, prepared pursuant to section 10 of the Federal Reserve Act and published in the Annual Report of the Board of Governors of the Federal Reserve System. This record includes not only the directives and the economic background therefor, but it also includes policy actions of the Committee with respect to transactions in bankers' acceptances, repurchase agreements covering Government securities, and various continuing statements of policy. The attached sheet contains references to the pages of the Board's Annual Report for the years 1951-1956 on which these instructions and policy guides are contained and discussed.

"You also requested a copy of the letter sent to the Presidents of all Federal Reserve Banks under date of August 3, 1955 concerning repurchase agreements, along with instructions and policy statements relating to this subject before and after August 2, 1955. As indicated above, the policy decisions regarding repurchase agreements are included in the Record of Open Market Policy Actions published in the Annual Report of the Board of Governors of the Federal Reserve System. Actions relating to repurchase agreements are recorded in the Annual Reports under dates of October 4, 1951 (page 107); September 25, 1952 (page 97); March 4-5, 1953 (page 91); June 23, 1954 (page 96); August 2, 1955 (page 102); and March 6, 1956 (page 24, first paragraph under Item 3, Review of Continuing Authorities or Statements of Policy.) A copy of the letter

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"of August 3, 1955 to the Presidents of all Federal Reserve Banks transmitting essentially the information given in the policy record entry for the same date is also enclosed in accordance with your request.

"Another request was that we furnish you with sample copies of the weekly report of the Manager of the System Open Market Account, plus a description of other reports made at regular intervals. Two of the weekly reports prepared during the calendar year 1956 are enclosed--those for the weeks ending May 23 and June 20. Because of the nature of these reports, their contents should be held confidential.

"Reports in substantially the same form as the weekly report are prepared prior to each meeting of the Federal Open Market Committee. The Manager of the System Account prepares these reports of open market transactions to cover the interval since the most recent meeting of the Committee. They are brought to date on the morning of the meeting by a supplemental report from the Manager.

"Among the reports prepared and distributed to members of the Federal Open Market Committee is a monthly statement showing the volume of transactions in United States Government securities and in bankers' acceptances, both outright and under repurchase agreement, with dealers under authorizations of the Federal Open Market Committee. An annual report covering operations of the securities function of the Bank designated to execute transactions for the System Account is prepared early each year. Also, the Manager of the System Open Market Account periodically prepares a report containing financial and operating data regarding individual dealers in United States Government securities. This report is compiled from information provided in strictest confidence. It is confidential and the Committee would not be in position to release it.

"While not falling strictly within the description of reports, members of the Committee are kept informed by telegrams in the course of the day concerning activity in the Government securities market and operations for the System Account.

"I believe that this letter comments on all of the matters mentioned in your several letters having to do with Open Market Committee matters. The other questions which you presented such as those relating to waiver of penalties for deficiencies in reserve requirements, audit and examination reports, expenses of the Federal Reserve Banks, and transactions in Government securities for member banks and others, either have been or will be covered in separate letters."

Mr. Balderston stated that he believed it would be helpful to have Mr. Riefler comment along lines of a statement that he had made

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before the directors of the Federal Reserve Bank of Chicago last week concerning a number of the arguments presented by critics of the System's current credit policies at the recent hearings before the Senate Finance Committee.

Mr. Riefler summarized his comments having to do with the following propositions or assertions: (1) that higher interest rates account for an important part of the inflation of prices; (2) that the American economy today is not characterized by a shortage of manpower, since unemployment is one-third higher than in 1952 when prices were stable; (3) that the American economy today is not confronted with a shortage of physical capacity to produce since new capacity has been and still is being greatly enlarged; (4) that consumer disposable income, in terms of real purchasing power, has not grown during the past year; and (5) that it is generally recognized that more production is the best cure for inflation.

Mr. Riefler stated that the first of these assertions was now being less confidently asserted than when the hearings began. Statistics presented at the hearings showed that interest costs were in fact a very small proportion of total business expense, and these statistics had made this assertion a pretty farfetched one. He then commented on the remaining four principal assertions, pointing out their respective pitfalls. Given assent to these four assertions, he said, the conclusion followed that measures to stimulate consumer spending, rather than saving, would so increase the output of goods and services, for

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which both manpower and capacity are available, as to cure inflation. This conclusion really asserts that the creation of more money, by increasing the demand for output, would curb inflation.

Mr. Riefler went on to say that the logical validity of any conclusion could be tested by stating it in reverse. In this case, the reverse proposition would be that the sure way to cure a deflation would be to raise interest rates and force contraction of the money supply. However, such logical refutation of the main conclusion does not meet the need for refuting each of the assertions separately, he said, and he then commented more fully on each of these four assertions.

After Mr. Riefler had concluded his remarks, Mr. Allen stated that following the presentation of these points by Mr. Riefler at the meeting of the Chicago Bank's Board of Directors, three of the directors asked whether the statement could be prepared in written form for distribution to interested persons. He suggested that it would be desirable if Mr. Riefler would do this, and Mr. Riefler stated that he would prepare a summary of his comments.

Secretary's note: In accordance with the foregoing, a summary of Mr. Riefler's comments was distributed under date of September 12, 1957.

During a brief discussion of the comments Mr. Riefler had made and of the desirability of improving public understanding of the points discussed, Mr. Hayes stated that yesterday the Federal Reserve Bank of New York started a series of sessions with leading businessmen in the


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area in which such men would be invited to the Bank in groups of about ten in number, to have luncheon and to spend a couple of hours discussing Federal Reserve policies and related matters. He was encouraged with the first meeting in that these men, who were from the top executive group, showed complete agreement with what the System was doing. Mr. Hayes stated that it was also contemplated that businessmen who were not necessarily in the top executive positions would also be invited to participate in similar sessions at a later stage.

It was agreed that the next meeting of the Committee would be held at 10:00 a.m. on Tuesday, October 1, 1957.

Thereupon the meeting adjourned.


Secretary