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, March 4, 1958, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Hayes, Vice Chairman
Mr. Balderston
Mr. Fulton
Mr. Irons
Mr. Leach
Mr. Mangels
Mr. Mills
Mr. Shepardson
Mr. Szymczak
Mr. Vardaman

Messrs. Erickson, Allen, Johns, and Deming, Alternate Members of the Federal Open Market Committee

Messrs. Bopp, Bryan, and Leedy, Presidents of the Federal Reserve Banks of Philadelphia, Atlanta, and Kansas City, respectively

Mr. Riefler, Secretary
Mr. Thurston, Assistant Secretary
Mr. Sherman, Assistant Secretary
Mr. Hackley, General Counsel
Mr. Solomon, Assistant General Counsel
Mr. Thomas, Economist
Messrs. Daane, Hostetler, Marget, Roelse, Walker, and Young, Associate Economists
Mr. Rouse, Manager, System Open Market Account
Mr. Carpenter, Secretary, Board of Governors
Mr. Kenyon, Assistant Secretary, 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

Mr. Swan, First Vice President, Federal Reserve Bank of San Francisco; Messrs. Abbott, Ellis, Mitchell, and Tow, Vice Presidents of the Federal Reserve Banks of St. Louis, Boston, Chicago, and Kansas City, respectively; Mr. Parsons, Director of Research, Federal Reserve Bank of Minneapolis; Messrs. Anderson and Atkinson, Economic Advisers, Federal Reserve Banks of Philadelphia and Atlanta, respectively

Mr. Riefler reported that advices of the election by the Federal Reserve Banks for a period of one year commencing March 1, 1958, of members and alternate members of the Federal Open Market Committee had been received and that each newly elected member and alternate member had executed the required oath of office. The members and alternate members were as follows:

Alfred Hayes, President of the Federal Reserve Bank of New York, with William F. Treiber, First Vice President of the Federal Reserve Bank of New York, as alternate member;

Hugh Leach, President of the Federal Reserve Bank of Richmond, with J. A. Erickson, President of the Federal Reserve Bank of Boston, as alternate member;

Wilbur D. Fulton, President of the Federal Reserve Bank of Cleveland, with Carl E. Allen, President of the Federal Reserve Bank of Chicago, as alternate member;

Watrous H. Irons, President of the Federal Reserve Bank of Dallas, with D. C. Johns, President of the Federal Reserve Bank of St. Louis, as alternate member;

H. N. Mangels, President of the Federal Reserve Bank of San Francisco, with Frederick L. Deming, President of the Federal Reserve Bank of Minneapolis, as alternate member.

Upon motion duly made and seconded, and by unanimous votes, the following officers of the Federal Open Market Committee were elected to serve until the election of their successors at the first meeting of the Committee after February 28, 1959, with the understanding that in the event of the discontinuance of their official connection with the Board of Governors or with a Federal Reserve Bank, as the case might be, they would cease to have any official connection with the Federal Open Market Committee:

Wm. McC. Martin, Jr.	Chairman
Alfred Hayes	Vice Chairman
Winfield W. Riefler	Secretary
Elliott Thurston	Assistant Secretary
Merritt Sherman	Assistant Secretary
Howard H. Hackley	General Counsel
Frederic Solomon	Assistant General Counsel
Woodlief Thomas	Economist
J. Dewey Daane, L. Merle Hostetler, Arthur W. Marget, Harold V. Roelse, Charls E. Walker, Oliver P. Wheeler, and Ralph A. Young	Associate Economists

Upon motion duly made and seconded, and by unanimous vote, the Federal Reserve Bank of New York was selected to execute transactions for the System Open Market Account until the adjournment of the first meeting of the Committee after February 28, 1959.

Mr. Hayes stated that the Board of Directors of the Federal Reserve Bank of New York had selected Mr. Rouse as Manager of the System Open Market Account, subject to the selection of the Federal Reserve Bank of New York by the Federal Open Market Committee as the Bank to execute transactions for the System Account and his approval by the Federal Open Market Committee.

Mr. Leedy entered the room at this point.

Chairman Martin said that in order to make certain there was no misunderstanding as to his position regarding the selection of the Manager of the System Account, he would read from the minutes of the meeting of the Committee held on March 6, 1956 the statement he made at that time in connection with the approval of Mr. Rouse as Manager. This statement was:

> "Chairman Martin stated that he was voting for approval of Mr. Rouse as Manager of the System Open Market Account although he disapproved of the procedure now followed by the Committee under which the board of directors of the agent Federal Reserve Bank selects the manager. There were no personalities involved in this feeling, the Chairman said, but he referred to the action of the Committee in authorizing appointment of a special committee at the meeting on March 2, 1955, to study and bring back to the Committee concrete proposals for perfecting the structural and operating organization that would best implement the policies of the Federal Open Market Committee. This committee, he said, had met with the Board of Directors of the New York Bank last November but he, as Chairman of the committee, had not called a meeting since that time partly, at least, because of pressure of other problems. Chairman Martin said that he intended to continue the committee appointed pursuant to that authorization until it had a report to submit to the full Committee, and in this connection he stated that he proposed to have a meeting of the committee on the day on which the next meeting of the Federal Open Market Committee (probably to be held on Tuesday, March 27, 1956) took place."

Chairman Martin went on to say that the Committee that had met with the Directors of the New York Bank in November 1955 had not met recently but he would propose that it continue in existence and that an effort be made to resolve this problem during the coming year. His purpose in mentioning the matter at this time was to reserve the position he had expressed two years ago and to say that in his opinion a more desirable and proper procedure would be for the Federal Open Market Committee to select the Manager of the System Open Market Account with the understanding that the Agent Bank would accept or reject that selection by the Committee. With this comment, he suggested that the Committee approve the selection of Mr. Rouse as Manager of the System Open Market Account.

Following a discussion, upon motion duly made and seconded, and by unanimous vote, the selection of Mr. Rouse as Manager of the System Open Market Account was approved.

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meetings of the Federal Open Market Committee held on January 28 and February 11, 1958, were approved.

Upon motion duly made and seconded, and by unanimous vote, the action taken by the members of the Federal Open Market Committee under date of February 25, 1958, authorizing that the target for free reserves be increased from \$200-\$300 million, as established at the February 11 meeting, to between \$400 and \$500 million during the period from February 25 to the next meeting of the Committee, subject to the usual qualifications, was approved, ratified, and confirmed.

Chairman Martin referred to a memorandum that had been distributed under date of February 28, 1958, relating to the procedure authorized at the meeting on March 2, 1955, whereby, in addition to members and officers of the Committee and Reserve Bank Presidents not currently members of the Committee, minutes and other records could be made available to any other employee of the Board of Governors or of a Federal Reserve Bank with the approval of a member of the Committee or other Reserve Bank President, with notice to the Secretary. At the Chairman's request, the Secretary commented briefly on the procedure, indicating that the list of authorizations would be reviewed with the members of the Committee and the Reserve Bank Presidents in order to make certain that it was current.

Thereupon, the procedure was reaffirmed without change.

The Chairman next referred to the resolution adopted by the Federal Open Market Committee on November 20, 1936 authorizing each Reserve Bank to purchase and sell, at home and abroad, cable transfers and bills of exchange and bankers' acceptances payable in foreign currencies to the extent that such purchases and sales may be deemed to be necessary or advisable in connection with the establishment, maintenance, operation, increase, reduction, or discontinuance of accounts of Federal Reserve Banks in foreign countries.

It was agreed unanimously that no action should be taken at this time to amend or terminate the resolution of November 20, 1936.

Before this meeting there had been sent to the members of the Committee a memorandum dated February 7, 1958, from Mr. Rouse and Mr. Leonard, Director of the Board's Division of Bank Operations, with respect to allocation of securities in the Open Market Account under the procedure that became effective September 1, 1953, pursuant to the action taken by the Committee at the meeting on June 11, 1953. There had also been distributed a tabulation containing a pro forma reallocation based on the ratios of each Reserve Bank's average total assets to the total for all Reserve Banks for the period March 1, 1957-February 28, 1958.

It was agreed unanimously that no action should be taken at this time to amend or terminate the procedure for allocation of securities in the System Open Market Account, as adopted pursuant to the action of the Committee on June 11, 1953.

Unanimous approval was given to the distribution of the weekly report of open market operations prepared at the Federal Reserve Bank of New York as follows:

1. The members of the Board of Governors
2. The Presidents of the 12 Federal Reserve Banks
3. Officers of the Federal Open Market Committee
4. The Secretary of the Treasury
5. The Under Secretary of the Treasury
6. The Assistant Secretary of the Treasury working on debt management problems
7. The Fiscal Assistant Secretary of the Treasury
8. The Chief of the Division of Bank Operations of the Board of Governors
9. The officer in charge of research at each of the Federal Reserve Banks not represented by its President on the Federal Open Market Committee

10. The alternate member of the Federal Open Market Committee from the Federal Reserve Bank of New York; the two Assistant Vice Presidents of the Federal Reserve Bank of New York working under the Manager of the System Account; the Managers of the Securities Department of the New York Bank; the Vice President, the Assistant Vice President and the Manager of the Research Department of the New York Bank; and the confidential files of the New York Bank pertaining to Federal Open Market Committee matters.
11. With the approval of a member of the Federal Open Market Committee or any other President of a Federal Reserve Bank, with notice to the Secretary, any other employee of the Board of Governors or of a Federal Reserve Bank.

Unanimous approval was given to the continuation of the authorization given by the Committee at its meeting on March 5, 1957 to the Manager of the System Account to engage in transactions on a cash as well as a regular delivery basis.

Chairman Martin next referred to the authorization to the Federal Reserve Bank of New York to purchase bankers' acceptances and to enter into repurchase agreements therefor, last approved at the meeting of the Committee on March 5, 1957. The present authorization provided for transactions by the New York Bank with acceptance dealers, and the Manager of the System Account had suggested in a letter to the Secretary dated February 27, 1958 that this authorization be amended so that it would also permit the New York Bank to purchase and sell bankers' acceptances direct from and to foreign accounts of that Bank.

Mr. Mills made a statement in which he expressed the view that the proposed broadening of the authority would run counter to what he understood to be the policy of the Committee to broaden the market for bankers' acceptances. After noting that the System portfolio now was just short of $42 million and that there was a strong demand for bankers' acceptances, Mr. Mills expressed the view that a broader market would be developed by the release of some portion of the acceptances now held by the System. He also said that it had been his thought that System holdings of bankers' acceptances represented a cushion to pick up the floating supply and that it would not be regarded, as would holdings of Treasury bills, primarily as a vehicle for the conduct of credit policy. Mr. Mills said that he would argue against adoption of the recommendation for broadening the authority and would prefer that the New York Bank deal solely in the established market for bankers' acceptances.

Mr. Hayes said that the suggested change would permit the New York Bank to effect transactions when the market was not in a position to have orders from foreign accounts completed conveniently for the market. For example, if a foreign holder gave a sizable sell order and acceptance dealers at that time had a heavy inventory and were not interested in buying the acceptances, it would be difficult to carry out the foreign bank's order. Mr. Hayes stated that if dealers were receptive the Bank would, of course, go to them and that use of the broadened authority would be a means of carrying through a transaction when the market was not receptive.

There followed a general discussion of the points raised by Mr. Mills and of the views expressed by Mr. Hayes, during which most of the comments indicated a favorable disposition toward changing the authorization to permit transactions with foreign accounts of the New York Bank as well as with acceptance dealers.

Chairman Martin stated that he doubted whether an important element of credit policy was involved, that he had been favorable to participation in the bankers' acceptance market primarily on the basis of being friendly to the market and because he thought it important to develop foreign trade, and that it seemed to him that it would be proper to permit the additional authority requested. If, however, any member of the Committee wished to have more time to study the question it could be held over until a later meeting. A number of the members of the Committee indicated that they would prefer to act on the question at the present time.

> Thereupon, upon motion duly made and seconded, the authorization for transactions in bankers' acceptances was approved in the following form, including authority for the Federal Reserve Bank of New York to buy from and sell to foreign accounts of that Bank.
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> Votes for this action: Messrs. Martin, Chairman, Hayes, Vice Chairman, Balderston, Fulton, Irons, Leach, Mangels, Shepardson, Szymczak, and Vardaman. Vote against this action: Mr. Mills.

The Federal Open Market Committee hereby authorizes the Federal Reserve Bank of New York for its own account to buy from and sell to acceptance dealers and foreign accounts maintained at the Federal Reserve Bank of New York, at market rates of discount, prime bankers' acceptances of the kinds designated in the regulations of the Federal Open Market Committee, at such times and in such amounts as may be advisable and consistent with the general credit policies and instructions of the Federal Open Market Committee, provided that the aggregate amount of such bankers' acceptances held at any one time by the Federal Reserve Bank of New York shall not exceed $50 million and provided further, that such holdings shall not be more than 10 per cent of the total of bankers' acceptances outstanding as shown in the most recent acceptance survey conducted by the Federal Reserve Bank of New York.

The Federal Open Market Committee further authorizes the Federal Reserve Bank of New York to enter into repurchase agreements with nonbank dealers in bankers' acceptances covering prime bankers' acceptances of the kinds designated in the regulations of the Federal Open Market Committee, subject to the same conditions on which the Federal Reserve Bank of New York is now or may hereafter be authorized from time to time by the Federal Open Market Committee to enter into repurchase agreements covering United States Government securities, except that the maturities of such bankers' acceptances at the time of entering into such repurchase agreements shall not exceed six months, and except that in the event of the failure of the seller to repurchase, such acceptances shall continue to be held by the Federal Reserve Bank or shall be sold in the open market. Such repurchase agreements shall be at the same rate as that applicable, at the time of entering into such agreements, to repurchase agreements covering United States Government securities.

The Committee approved by unanimous vote a renewal of the following authorization to the Federal Reserve Bank of New York to enter into repurchase agreements with nonbank dealers in Government securities:

1. Such agreements
   (a) In no event shall be at a rate below whichever is the lower of (1) the discount rate of the

Federal Reserve Bank on eligible commercial paper, or (2) the average issuing rate on the most recent issue of three-month Treasury bills;

(b) Shall be for periods of not to exceed 15 calendar days;

(c) Shall cover only Government securities maturing within 15 months; and

(d) Shall be used as a means of providing the money market with sufficient Federal Reserve funds to avoid undue strain on a day-to-day basis.

2. Reports of such transactions shall be included in the weekly report of open market operations which is sent to the members of the Federal Open Market Committee.
3. In the event Government securities covered by any such agreement are not repurchased by the dealer pursuant to the agreement or a renewal thereof, the securities thus acquired by the Federal Reserve Bank of New York shall be sold in the market or transferred to the System Open Market Account.

At the meeting on December 3, 1957, the Committee approved a recommendation from the Manager of the System Open Market Account and the Secretary of the Committee that the rate charged on special short-term certificates of indebtedness purchased direct from the Treasury pursuant to paragraph (2) of the Committee's directive to the Federal Reserve Bank of New York be fixed at 1/4 of 1 per cent below the discount rate of the Federal Reserve Bank of New York at the time of such purchase.

No action was taken to amend or terminate this authorization for fixing the rate on special short-term certificates of indebtedness purchased direct from the Treasury.

On March 1, 1951, and at the annual meeting in March of each year since, the Committee had authorized the Chairman to appoint a

Federal Reserve Bank as agent to operate the System Account temporarily in case the Federal Reserve Bank of New York was unable to function. The report of the Subcommittee on Defense Planning dated January 9, 1956, which was approved by the Federal Open Market Committee on January 10, 1956, included a recommendation that this authorization be reaffirmed, and such action was taken on March 6, 1956, and March 5, 1957.

Mr. Vardaman suggested that it would be desirable to have the authorization reviewed for the purpose of ascertaining whether any change was needed to make clear that it extended to the Acting Chairman of the Committee in the event the Chairman was not available.

Thereupon, the authority to the Chairman to appoint a Federal Reserve Bank as agent to operate the System Account temporarily in case the Federal Reserve Bank of New York was unable to function was reaffirmed, with the understanding that Mr. Vardaman's suggestion would be followed.

The following resolution to provide for the continued operation of the Federal Open Market Committee during an emergency was then reaffirmed by unanimous vote:

In the event of war or defense emergency if the Secretary or Assistant Secretary of the Federal Open Market Committee (or in the event of the unavailability of both of them, the Secretary or Acting Secretary of the Board of Governors of the Federal Reserve System) certifies that as a result of the emergency the available number of regular members and regular alternates of the Federal Open Market Committee is less than seven, all powers and functions of the said Committee shall be performed and exercised by, and authority to exercise such powers and functions is hereby delegated to, an Interim Committee, subject to the following terms and conditions.

Such Interim Committee shall consist of seven members, comprising each regular member and regular alternate of the Federal Open Market Committee then available, together with an additional number, sufficient to make a total of seven, which shall be made up in the following order of priority from those available: (1) each alternate at large (as defined below); (2) each President of a Federal Reserve Bank not then either a regular member or an alternate; (3) each First Vice President of a Federal Reserve Bank; provided that (a) within each of the groups referred to in clauses (1), (2), and (3) priority of selection shall be in numerical order according to the numbers of the Federal Reserve Districts, (b) the President and the First Vice President of the same Federal Reserve Bank shall not serve at the same time as members of the Interim Committee, and (c) whenever a regular member or regular alternate of the Federal Open Market Committee or a person having a higher priority as indicated in clauses (1), (2), and (3) becomes available he shall become a member of the Interim Committee in the place of the person then on the Interim Committee having the lowest priority. The Interim Committee is hereby authorized to take action by majority vote of those present whenever one or more members thereof are present, provided that an affirmative vote for the action taken is cast by at least one regular member, regular alternate, or President of a Federal Reserve Bank. The delegation of authority and other procedures set forth above shall be effective only during such period or periods as there are available less than a total of seven regular members and regular alternates of the Federal Open Market Committee.

As used herein the term "regular member" refers to a member of the Federal Open Market Committee duly appointed or elected in accordance with existing law; the term "regular alternate" refers to an alternate of the Committee duly elected in accordance with existing law and serving in the absence of the regular member for whom he was elected; and the term "alternate at large" refers to any other duly elected alternate of the Committee at a time when the member in whose absence he was elected to serve is available.

Unanimous approval was also given to a renewal of the resolution set forth below authorizing certain actions by the Federal Reserve Banks during an emergency.

The Federal Open Market Committee hereby authorizes each Federal Reserve Bank to take any or all of the actions set forth below during war or defense emergency when such Federal Reserve Bank finds itself unable after reasonable efforts to be in communication with the Federal Open Market Committee (or with the Interim Committee acting in lieu of the Federal Open Market Committee) or when the Federal Open Market Committee (or such Interim Committee) is unable to function.

(1) Whenever it deems it necessary in the light of economic conditions and the general credit situation then prevailing (after taking into account the possibility of providing necessary credit through advances secured by direct obligations of the United States under the last paragraph of section 13 of the Federal Reserve Act), such Federal Reserve Bank may purchase and sell obligations of the United States for its own account, either outright or under repurchase agreement, from and to banks, dealers, or other holders of such obligations.

(2) In case any prospective seller of obligations of the United States to a Federal Reserve Bank is unable to tender the actual securities representing such obligations because of conditions resulting from the emergency, such Federal Reserve Bank may, in its direction and subject to such safeguards as it deems necessary, accept from such seller, in lieu of the actual securities, a "due bill" executed by the seller in form acceptable to such Federal Reserve Bank stating in substantial effect that the seller is the owner of the obligations which are the subject of the purchase, that ownership of such obligations is thereby transferred to the Federal Reserve Bank, and that the obligations themselves will be delivered to the Federal Reserve Bank as soon as possible.

(3) Such Federal Reserve Bank may in its discretion purchase special certificates of indebtedness directly from the United States in such amounts as may be needed to cover overdrafts in the general account of the Treasurer of the United States on the books of such Bank or for the temporary accommodation of the Treasury, but such Bank shall take all steps practicable at the time to insure as far as possible that the amount of obligations acquired directly from the

> United States and held by it, together with the amount of such obligations so acquired and held by all other Federal Reserve Banks, does not exceed $5 billion at any one time.
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> Authority to take the actions above set forth shall be effective only until such time as the Federal Reserve Bank is able again to establish communications with the Federal Open Market Committee (or the Interim Committee), and such Committee is then functioning.

Before this meeting there had been distributed to the members of the Committee a report of open market operations covering commitments executed February 11, 1958, through February 26, 1958, and a supplementary report covering commitments executed February 27 through March 3, 1958. Copies of both reports have been placed in the files of the Federal Open Market Committee.

Mr. Rouse reported that there had been remarkable fluctuations in bill rates since the February 11 meeting. The bills auctioned on February 17 went at an average rate of 1.73 per cent, but the rate dropped to 1.20 per cent in the following week and then rose to 1.35 per cent on March 3. There was a long tail in the auction yesterday, with the stop-out price at 1.40 per cent. The sharp drop in the rate on February 24 was due to expectations of a large demand for bills from some State funds, from the telephone company, and from commercial banks employing reserves released by the reduction in reserve requirements. This buying did not materialize in the expected volume, and bills instead had come into the market from foreign accounts, the System Account, and State funds. Mr. Rouse also reported that the market was now entering the period when corporate tax selling would pick up and, as a result, there had been a build-up in dealers' bill positions. Positions totaled $750 million on February 28, and dealers were awarded $550 million new bills yesterday. Bank dealers held most of this supply of bills, and nonbank dealers' holdings appeared to be firmly placed, Mr. Rouse said, so there was no reason for real concern in spite of the large supply. One factor in the market at the present was that Chicago banks were stockpiling bills, apparently for the April 1 personal property tax assessment date. In Mr. Rouse's judgment, the recent backup in bill rates was a healthy development.

Turning to the recent Treasury financing, Mr. Rouse said that the cash offering was a success, with large subscriptions by both bank and nonbank purchasers. The allotment was expected to be less than 25 per cent.

On bond markets generally, Mr. Rouse reported that there had not been much change in prices of seasoned bonds, but reoffering rates on new issues had tended to rise in recent days. As he had reported at earlier meetings, there was a good deal of speculation in bonds following the reduction in discount rates in November. The momentum of this speculative demand had driven new issue rates down to the 3.60 per cent range on Aaa corporate utility issues by late January; a Aaa utility was reoffered in the last few days to yield 3.94 per cent and had moved slowly at that rate. "Aa" new issue rates had moved well above 4 per cent and A rates were 4.25 per cent. A similar situation had developed in the municipal market, where dealers' inventories had climbed to a record high. Short-term municipal obligations had sold well, particularly to banks, but long maturities had moved slowly. Mr. Rouse said that exceptional factors had caused bond prices to move higher than could be supported by the supply of investment funds available to buy them, and the present consolidation and upward movement of rates was necessary to establish balance in the market. Sharply easier credit policy aimed at improving the capital markets by supplying bank reserves would not promise to do too much good.

At the conclusion of Mr. Rouse's report, Mr. Allen reported that he had encountered instances of speculation in bonds that supported what Mr. Rouse had said.

> Upon motion duly made and seconded, and by unanimous vote, the transactions for the System Account during the period February 11, 1958, through March 3, 1958, were approved, ratified, and confirmed.

At Chairman Martin's request, Mr. Young made a statement on the economic situation supplementary to the staff memorandum distributed under date of February 28, 1958. Mr. Young's comments were substantially as follows:

> Economic activity through February continued to recede, with adverse weather conditions accentuating the decline.

The February decline in industrial production was evidently about 2 index points, and possibly larger, carrying the Board's index at least to 131, or 10 per cent under last summer's high. The further decline was distributed among durable and nondurable manufacturing lines and mining and petroleum. Output curtailment in the automobile industry was a special feature of the month. Reflecting increased demands for heating associated with the unusually cold weather, output of electricity and gas picked up considerably.

Construction activity, after seasonal adjustment, continued close to fall levels, with commercial construction down further, public utility construction up further, and residential and public construction little changed. Highway work was off more than allowed for in the existing seasonal adjustment and this accounted for an apparent moderate falloff in total construction activity. Housing starts in January continued at just over a million units, the level sustained since the middle of last year.

Employment has continued to decline and unemployment to rise. Initial unemployment benefit claims in the week ending February 22 were close to half a million, or double the number a year earlier. Continued claims reached 3.1 million--a record level.

The mid-February unemployment estimate has just been made available to the Committee on a confidential basis, prior to public release by a week or more. It shows a figure of 5.2 million, up 670,000 from January and 2 million from a year ago. The normal seasonal movement for January to February is little changed, and a 5.2 million unemployed figure is a postwar high. Related to the labor force on a seasonally adjusted basis, the unemployment percentage comes out at 6.7 per cent, about as high a rate as reached in 1949.

Also, preliminary Commerce Department estimates of inventory change and orders for January were made available to us yesterday on a confidential basis. They show a January inventory liquidation of $600 million, mostly in durable goods lines. The estimated January decline compares with declines of $350 million in December, $232 million in November, $63 million in October, and $37 million in September.

New orders and unfilled orders both declined in January. The amount of decline for unfilled orders--$1.5 billion--was close to the average of recent months.

Retail sales estimates for January are now being lowered to the December level, in place of the earlier estimate of a significant gain over December. According to department store sales figures in February, retail trade has worsened sharply.

While unfavorable shopping weather was a factor in much of the country, declines were also marked in areas in which weather conditions were not severely adverse.

Automobile sales dropped particularly sharply. In the first ten days of February deliveries were off 15 per cent from January and 29 per cent from a year ago. Deliveries in the second ten days--the period of the most adverse weather--were off appreciably further. Dealer stocks of domestic cars rose to 886,000 on February 20, a fourth above a year ago. A responsible industry source called yesterday and reported confidentially that daily sales of new cars in the last ten days of February had shown no improvement from the second ten days.

Used car sales were also off sharply in February, running about 8 per cent under January and 18 per cent under last February.

Cash sales of automobiles have apparently fallen off much more than instalment sales. Preliminary figures on instalment credit show a January rise of about $100 million on a seasonally corrected basis. New car repossessions have evidently reached a very high level, attaining a rate of one in 10 for one large national finance company. This is the highest rate for this company since the early thirties.

The housing market appears to hold fairly strong. Markets for existing houses remain active and the number of unsold new houses has held fairly steady at a moderate figure. Easier credit conditions have been reflected in some increase in mortgage market activity. Offerings to FNMA for immediate purchase have continued to decline and recently the volume of mortgages sold by FNMA has increased markedly. Applications to FHA for insurance on new houses rose appreciably in January and the rate was two-thirds above a year earlier.

Wholesale prices have risen recently, reaching a new high at the end of February, about one per cent above the average of the fourth quarter. With price averages for industrial commodities little changed, the increase mainly reflects higher prices for farm products and foods, notably livestock, meats, vegetables, and fruits. Price movements of industrial materials have been quite selective and the average has been showing little change. The most recent purchasing agents' roundup indicates that lower materials prices are beginning to work through to fabricated items and that discounts from list prices are increasingly encountered.

Mainly reflecting higher food prices but also some further advances in prices of services, the consumer price index for January showed a rise of .6 per cent. With wage and salary incomes declining further, this increase accentuated the falloff in consumers' real income. In March, approximately 1.3 million industrial workers will receive a 2-to-3 cent an hour wage increase to compensate for this cost-of-living advance.

Most observers agree that the extent and duration of the present recession is heavily dependent on the course of business capital expenditures. Two items of advance release information have become available indicative of the course of these expenditures.

The first relates to the Newsweek-NICB survey of capital appropriations by large manufacturing corporations for the fourth quarter. These appropriations were reported to be one-third smaller than a year earlier. Cancellations of previously approved appropriations were substantial, and the backlog of appropriations declined more than a fifth.

The second item relates to the Commerce-SEC plant and equipment expenditure survey for the second quarter and calendar year. This survey is not completely tabulated, but preliminary indications point to a decline in expenditures for the year of as much as 10 per cent. The McGraw-Hill survey of last fall indicated a year-to-year decline of 7 per cent.

This preliminary information about the indications of these two surveys should be held confidential until public release.

Economic news from abroad has both encouraging and discouraging aspects. In Western Europe, economic activity appears to continue at high levels, with no clear signs of deterioration, except financially for France. In Canada, recent data suggest a leveling out of recession. In Japan, financial adjustment seems in process of being effected without serious cutback in productive activity. In various other countries in Latin America and the Far East, internal inflationary pressures are very strong and balance of payments problems are becoming still more acute. United States exports continued to decline through December, but imports have remained close to the level of the past two years.

By way of conclusion to today's economic summary, one can say that it is a report of little cheer. The most recent facts clearly suggest that the 1957-58 recession has a better than even chance of being less moderate in extent and duration than either the 1948-49 recession or the 1953-54 recession.

Mr. Thomas summarized recent financial developments as follows:

While business activity has been showing definite indications of deepening recession, bank credit has been expanding and borrowing in general was held up at a high level. This contrast may be directly attributable to the Federal Reserve policy of maintaining a generous supply of bank reserves. Business borrowing at banks, it is true, has been sharply reduced, but banks supplied with ample reserves, have expanded other types of credit by amounts that far exceeded the business loan liquidation while reducing their borrowings at the Reserve Bank to a negligible volume. Total deposits at banks have increased in a period when they usually decline seasonally. It would seem likely that deposit turnover declined in February, but the January figures, the latest available, held at close to the fourth quarter average.

To appraise the net effect in credit markets of the decline in business and the shift in monetary policy, comparisons need to be made with the latter part of November, in order to balance out the large offsetting seasonal movements in December and January. From November 27 to February 26, banks in leading cities increased their total loans and investments by about $1.1 billion, compared with decreases of about the same amount in the two previous December-February periods. Commercial loans and consumer loans both declined, showing a combined decrease of over $1-1/4 billion, compared with decreases aggregating less than a quarter billion in the same period a year ago and increases totaling over half a billion two years ago. Holdings of securities and loans on securities increased by over $2-1/4 billion this year, compared with decreases of well over half a billion last year and about $1.7 billion two years ago. Substantial portions of this year's increases occurred in February.

Demand deposits adjusted showed greater than seasonal decreases in December and January but partial data for February indicate a seasonally adjusted rise that partly offset the previous declines. In the past three months United States Government deposits have increased, compared with decreases in corresponding months of the two previous years. Time deposits showed a spectacular increase of nearly $2 billion this year--over twice last year's sharp expansion that followed the interest rate rise.

Since the growth in deposits has been in time accounts, the net result of these changes on total required reserves has been negligible, but the lack of change in required reserves compares with declines of over $500 million in the corresponding period a year ago and nearly $250 million two years ago. Banks have obtained funds from the usual seasonal return flow of currency, partly offset by other market factors, and have thus been able to reduce borrowings. This year, in contrast to other years, these additions to the reserve supply from market factors have not been offset by a reduction in Federal Reserve open market accounts. Last year those accounts showed a net drop in the three months of over $1.3 billion and two years ago a decline of nearly $600 million. Free reserves this year increased by nearly $600 million; in the same period last year they declined by $200 million.

It is evident from these facts that banks have been supplied with ample reserves and have used them not only to get out of debt but to expand credit contrary to usual seasonal trends. In the face of a liquidation of business loans, banks have found other uses for funds in securities and loans on securities.

One result of the easier reserve position has been the sharp decline in short-term interest rates. The rate on Treasury bills, which responds sensitively to changes in the supply of free reserves or when banks are in debt fluctuates around the discount rate, is now close to 1-1/4 per cent. This is at the average level that prevailed early in 1955 when free reserves were around $300 million. Treasury bill rates have almost reached the level at which nonbank buyers may be inclined to hold deposits rather than bills, as was the case in 1954. The low bill rate has induced substantial shifting of liquid balances into time deposits and led to a reduction in rates paid on such deposits by several leading banks.

Rates on bankers' acceptances and commercial paper have also been reduced to the lowest levels since early 1955. Rates on acceptances are now at a level relative to the prime loan rate that gives borrowers a substantial advantage to obtain funds through acceptances. Generally in the postwar period the advantage has been in favor of borrowers at the prime rate, when minimum balance requirements are ignored.

Long-term rates have also declined sharply, but not as much as medium and short-term rates, and they are still above levels generally prevailing prior to the autumn of 1956. Long-term rates do not as a rule respond as sensitively or as promptly as short rates to changes in availability of credit, but they have also been held up recently by the continued heavy volume of borrowing in the capital markets. New issues of securities by corporations and particularly by State and local governments have been so large that congestion has developed in capital markets. Recent offerings of long and medium-term securities by the Treasury and by Government agencies have absorbed some available funds in this sector of the market. In view of the existing exceptionally wide spread in the pattern of yields, it seems likely that in the course of time either short-term rates will rise or medium and long-term rates will decline further.

Figures of free reserves in February have been raised by $50 to $90 million above original estimates because required reserves at country banks were below preliminary estimates. The revised figures averaged a little over $300 million for the month. The average for this week is expected to exceed $450 million. After that the weekly average may be less than $400 million if usual seasonal trends are shown in the money supply and in other factors influencing the supply and use of reserve funds. To maintain a higher level will require System purchases of securities. It will be difficult to supply reserves through repurchase contracts as long as the repurchase rate is so far above market rates.

With the present levels of free reserves and of short-term interest rates, current Reserve Bank discount rates have no great significance. If member banks do find occasion to borrow, however, little is gained and something may be lost by making them pay current discount rates. If discount rates at or near this level should be appropriate at some later time, when a turn has occurred in business, the ability to raise rates at that time would probably have some advantage.

After a brief discussion of the comments by Mr. Thomas, Mr. Hayes presented the following statement of his views with respect to the business outlook and credit policy:

Recent statistical data confirm the continued business decline, and there is no sign yet of any combination of favorable factors sufficiently strong to reserve this trend. Besides the lower level of activity in many basic industries, there have recently been some indications of declines in nondurable goods output as well. Unemployment probably approached the 5,000,000 level in February--and personal income is apparently diminishing, after excluding the effect of a sharp dip in seasonally adjusted dividend income in December.

While consumers, businessmen and the stock market have shown notable restraint so far in the face of discouraging business developments, there is always a possibility that mass psychology will develop quite unfavorably if the adverse news that we look for in the next few weeks should be considered by the public as unexpected and startling. I have in mind such items as the February unemployment figures, S.E.C.-Commerce survey data on plant and equipment expenditures for 1958, and estimates of corporate profits for the fourth quarter of 1957, which may be sharply lower than the year before. Even allowing for the effect of bad weather in recent weeks, there are some signs that retail sales are beginning to reflect the increased unemployment, shorter hours, and lower actual and expected personal income. On the other hand, psychology is being buoyed to some extent by expectations of heavier defense outlays and, in some quarters, by hopes of the usual spring pick-up. Furthermore, it is also widely expected that if no clear signs of improvement appear within the next month or so, some major government remedial action will be forthcoming in the form of a tax cut or substantial public works expenditures or both.

The price picture remains paradoxical, with both wholesale and consumer indices showing some increase in spite of economic recession. It may be that the abandonment of fair trade price practices by General Electric and some of its major competitors may become an important influence in restoring greater price flexibility at the retail level. I have been disturbed by the evident rigidity of a large part of the price structure, which seems likely to delay materially the economic adjustments needed to permit resumption of economic growth. There is also ample ground to fear a resurgence of inflationary pressures in the longer run--but this clearly would not justify our failing to give primary attention now to efforts to counter a recession of unknown depth and duration, which seems likely to exceed in severity that of 1953-54.

I think we have already accomplished a good deal in the way of easier availability of bank credit and improved bank (and perhaps corporate) liquidity through the various measures taken since last fall. Bank credit continues to show little expansion except for Government security holdings, and the main effects of the change in monetary policy appear to have been in the capital issues market and, to some extent, in the mortgage market, neither of which, however, has so far shown sustained strength. We should see to it that monetary policy is contributing as much as it can to the recovery process.

Fortunately the Treasury should be out of the market until April, so that for the first time in many weeks we can plan the use of the various instruments of Federal Reserve credit policy on economic grounds alone.

With respect to open market operations, the projections suggest that a minimum of transactions will be needed in the next three weeks if, as I hope, the Committee is willing to retain the degree of ease represented by the target of approximately $400-$500 million of free reserves adopted last week to avoid large sales of bills which would have been inconsistent with the Board's action in lowering reserve requirements. It is hard to predict what level of free reserves will suffice, in view of the present fluidity of the national money market and short-term securities market, to provide adequate ease without creating a needlessly sloppy situation. With this in mind, I would be inclined to give the Manager wide leeway with respect to free reserves, with $500 million being looked upon as an upper limit in the absence of new and unexpected developments. I have been glad to note an increase in total reserves during February over last February's level, and our efforts should be directed toward widening this year-to-year growth in reserves (adjusted for changes in percentage requirements) and promoting growth in the money supply.

Turning to the matter of interest rates, I would first like to point to the steep yield curve which has been established in the last few weeks. Short-term market interest rates have been driven sharply lower by easy availability of bank reserves and by the reduction in supply of short-term Treasury securities resulting from the recent refunding. At the same time, the steadily large supply of new corporate and municipal issues, coupled with Treasury refunding and cash operations in the intermediate and long-term markets, have caused longer-term rates to reverse themselves and move higher. Although it is to be expected that eventually funds will gradually be drawn from the shorter market out through the maturity structure, I am rather concerned by the degree of restraint currently being applied by the congestion in the capital markets and the reversal in the downward trend of interest rates to would-be borrowers of long-term capital--a degree of restraint which seems scarcely consistent with current economic conditions or our own policies.

The spread that has developed between the 2-3/4 per cent discount rate and short-term market rates naturally gives rise to the question whether further action is called for on the discount rate. An additional cut would perhaps be consistent with recent open market and reserve requirement policies and might have the effect of triggering a further reduction in bank lending rates, which to date have responded only slowly and grudgingly to the change in System policy and are far out of line with short market rates. On the other hand, it can be argued that, with member bank borrowing already at a low level, it is doubtful whether a lower discount rate would induce banks to reduce lending rates and aggressively seek new loans. The last cut is only a little over a month old, and the reduction in reserve requirements scarcely a week old. There may be disadvantages in nibbling away at the discount rate with frequent small cuts so that if a major move should be considered necessary at some later date to cope with more critical economic circumstances, it would bring the discount rate down to a figure lower than would be consistent with an interest rate level conducive to adequate saving. To put it another way, there is something to be said in these circumstances for deliberately making the discount rate a relatively sluggish rate which will not necessarily reflect fully the more extreme swings in short-term market rates.

All things considered, I would think that the next reduction should not exceed 1/4 per cent and might well be deferred a bit longer, although it should probably occur before our next meeting.

Finally, as to the directive: I believe the time has come for the directive to give more explicit recognition of the established fact of the business recession and the switch in credit policy to a direct effort to provide an availability of money and credit that would help to counteract recessionary forces. Clause (b) in the directive might be amended to read as follows: "to combating economic recession."

Mr. Erickson said that the unemployment situation was bad in the First District, although the district was not quite as badly off as the national average in the year-to-year comparison for January. Department store sales, which were good during the first five weeks of the year, turned down in February and were now about 4 per cent behind last year. Automobile registrations for 1957 ran 5 per cent behind 1956, whereas the national average was slightly above 1956. Construction was running about 4 per cent ahead of January 1957.

One bright spot was that the ski resorts had been booming, with January business well ahead of the previous year. February also was a good month and March and April likewise were expected to be good. Advance registrations for boys' and girls' camps were 6 per cent higher than the good level of January a year ago. Loans at banks had been declining at about the same rate as last year, while the Reserve Bank discount window was being used only by the smaller banks.

Mr. Erickson said that he would favor a change in the Committee's directive and felt that it might contain some reference to monetary ease, a phrase that had been used at times in the past. Thus, clause (b) in paragraph (1) might have added to it "by continuing to maintain ease in the money market." He doubted that anything should be done about the discount rate until the Treasury financing was out of the way, but he would like to see the rate reduced another quarter per cent during March. As to open market operations, he would favor giving the Manager of the Account a certain amount of leeway. He would hold free reserves in the $350-$500 million range and agreed with Mr. Hayes that we should prevent a sloppy situation in the market.

Mr. Irons stated that Eleventh District conditions continued to trend downward slightly. The major exception was in the oil industry, where the situation had deteriorated badly and production was on a nine-day allowable basis. This meant that production of crude in March would be at a daily average rate of 2-1/2 million barrels, compared with a daily average of about 3.7 million barrels at the time of the Suez crisis and a plateau or "normal" of about 3.4 million excluding that period. The situation, which reflected imports from the Middle East and elsewhere, was having an effect not only on the oil and associated industries but also on State finances. Retail trade, which ran ahead of last year in January, was bad during the first two weeks of February and then increased in the third week with the result that the first seven or eight weeks of the year ran around 4 per cent below a year ago. Department stores gave various reasons for the decline, including bad weather and psychology, and there were indications that prices might be a factor because it had been found that whenever price-reduction sales were held, the response was excellent. Collections were not presenting a difficult problem. Employment in the district was down a bit further. The aircraft industry, which experienced a decline in the latter part of 1957 and was using up a backlog of orders, seemed to look forward to some improvement, and construction was holding up fairly well. In general terms and excluding the oil industry, one could say that the extent of the decline in the district would range from 2 to 5 per cent below a year ago. The decline in bank loans this year was appreciably less than a year ago, Mr. Irons said, the comparison being about $28 million against $67 million. Member banks were not borrowing significantly; the city banks had not been borrowing for some time, and the only borrowing at the Reserve Bank was by country banks for seasonal reasons. At the moment, banks had substantial aggregate free reserves. Heavy rains, particularly in the southern part of the district, produced a problem of getting people into the fields. Citrus prospects were very favorable, and on the whole the agricultural outlook was promising.

As to policy, Mr. Irons said that in view of the reduction in reserve requirements, it would be consistent to maintain free reserves at around the $400 million level, with a certain leeway given to the Manager of the Account. He was disturbed about the disparity between the discount rate and short-term market rates. If open market policy was correct and the reduction of reserve requirements was correct, one might question whether the discount rate policy was correct. He was not sure whether he would favor a reduction of a quarter or a half per cent at this time, but a reduction of the rate would move in the direction of being realistic. On balance, he felt that consideration might well be given to getting the discount rate better in line with the market. He hoped that any change would be in such an amount as not to stir up further speculation and anticipation, which might cause short-term rates to pull away from the discount rate even further. He would not object to a change in the directive to indicate a shift in policy.

Mr. Mangels said that the Twelfth District situation was a little different from that in some other areas. Preliminary employment data for December showed only a slight decline other than seasonal, decreases in manufacturing and mining employment being offset by gains in construction and trade. The decline in aircraft employment in January was only about 20-25 per cent of the average monthly decline from July through December. In Oregon, lumber employment had picked up somewhat. Although orders for plywood were up, prices had been reduced again to $64 per thousand feet, compared with $90 two years ago. The Oregon unemployment trust fund was now below the 3 per cent level and all experience rating credits had been cancelled. Therefore, for the first time since 1941, employers would be charged 2.7 per cent of covered wages until the fund was built up. Insured unemployment in January was unchanged from December, the third month of stability after four months of sharp decline. Department store and auto sales were down somewhat, and steel mills were operating at 65 per cent of capacity. Residential construction permits were up in January from January 1957. Demand for California citrus fruits was strong and orange and grapefruit prices were up. The cotton crop was excellent and domestic mills were paying higher prices than export customers. For the three weeks ending February 19, the decline in bank loans was double that of a year ago, Mr. Mangels said. Banks had funds to take care of all foreseeable loan demands, but demand had moderated somewhat.

Mr. Mangels said that it appeared that a period was approaching which would afford a good test of the flexibility of both business and labor to adjust to changing consumer demands. He believed that price cuts would be necessary to stimulate consumption, and while present excess capacity should bring about price declines, the latest consumer price index showed a further advance.

Mr. Mangels suggested that existing policy should not be changed. Free reserves in the $400-$500 million range would be about right for the next two weeks, he said, and he would have no objection to a change in the Committee's directive as suggested.

Mr. Deming said that the economic slide continued in the Ninth District during February. Unemployment was still rising during that month although it would normally level off in late February and remain stationary in March. This might not happen this year. If the movement of iron ore proved to be less than last year, unemployment would be greater this spring than for some time, Mr. Deming said, adding that the taconite plants in Minnesota were now planning to produce at 80 per cent of capacity this season compared with 100 per cent last year. This reflected a severe lack of demand in the iron ore industry. Although the rise in unemployment this year had been more severe than last, there were almost as many persons employed in the State of Minnesota at this time as a year ago. The two bright spots in the district continued to be found in agriculture, where cash income in 1957 was about 3 per cent higher than in 1956, and in home building, where the number of permits issued in January 1958 was a third higher than in

January 1957. Bank loans were about the same as last year, a decline in business loans having been mostly offset by an increase in loans of other types.

Mr. Deming said that he agreed with Mr. Hayes that the Committee should deal with the situation as it saw it today, rather than on the basis of a possible resumption of inflationary pressures. He had been impressed with the 4-1/2 million of unemployed at the time of the preceding meeting and he was more impressed with the 5 million unemployed reported by Mr. Young this morning. He would move toward the $500 million of free reserves cited as an upper range by Mr. Hayes. Mr. Deming said that he would favor a reduction of 1/2 per cent in the discount rate as soon as feasible. As a matter of fact, he would like to see a greater reduction in order to bring the rate better in line with the bill rate, but a greater reduction might be misinterpreted by the public. Mr. Deming agreed that the Committee's directive should be changed and, while he did not see a way of achieving it immediately, he would like to see reserve requirements further reduced.

Mr. Allen said that in the last few weeks business activity in the Seventh District appeared to have declined a little more than in the nation as a whole, because the automotive and industrial machinery industries continued to dominate the district situation. Supplementing Mr. Young's report on the poor record of automobile sales, Mr. Allen said that new car inventories of 887,000 on

February 20 represented 73 days supply, based on sales in the second days of the month of 12,149 per day. This was an industry figure, and at least some of the makes were in greater than 73 days supply. Optimistic straws noted by Mr. Allen included a slight improvement in orders for steel, improved demand for certain industrial goods such as welding rod, and some rehirings of a seasonal nature in the farm machinery industry. But the continued declines in automotive and industrial machinery production were dominating. Claims for unemployment insurance were being filed at a faster rate, relative to a year ago, in the Seventh District than in the nation. However, as of February 8 the proportion of covered workers receiving unemployment insurance was somewhat less than the national average in Illinois, Iowa, and Wisconsin. It was higher than the national average in Michigan and Indiana.

Department store results thus far available made it seem unlikely that February would maintain the rather good January rate of consumer buying, Mr. Allen said, adding that big ticket household items had been especially weak. On the other hand, consumers were showing less than expected resistance to high meat prices, and certain luxury goods such as cameras were moving well. The public seemed wary of purchases involving large outlays, particularly if credit was involved, although in the rural areas favorable farm prices and income trends were reported to be supporting relatively good levels of sales of retail goods and farm machinery. Steel firms reported some improvement in orders and their rate of production seemed to have stabilized. In January, however, ingot output was 40 per cent below last year, whereas metal fabricating was off only 11 per cent, which suggested a rapid liquidation of inventories. The size of the gap between use and production of steel indicated that steel output could rise moderately despite a continued decline in over-all industrial production. Bank debit figures for January from 32 metropolitan reporting areas were off 1 per cent from a year ago, but 19 of the 32 areas reported gains, with the largest gains in Iowa cities.

Mr. Allen reported that figures indicated savings were being well maintained, inflows to time accounts at commercial banks during January approximately matching January of 1957, while withdrawals were below a year ago. Little use of the discount window was being made by the larger district banks, in fact none of them borrowed last week. One of the largest banks had been a consistent buyer of Federal funds, but that bank now had a large portfolio of Treasury bills in preparation for the April 1 tax date. Doubtless there would be more bill accumulation during March and other banks would be buying funds or borrowing or both, but in recent years the district's banks had been getting away from their former practice of buying bills in January and carrying them until April. Rather, they pick up bills in March or they cover their problem through repurchase arrangements.

With regard to the directive, Mr. Allen said he had come to the meeting with the idea that the instruction for "mitigating recessionary tendencies" was not realistic, and he still felt that way. He had had in mind language such as Mr. Hayes suggested but perhaps a more positive phrase such as "promoting economic recovery" would be better. As to the discount rate, the Chairman of the Chicago Bank had commented yesterday that he did not think he would want to do anything until the first week in April, when the results of the Easter business were known. Mr. Allen expressed the view that the discount rate had lost much of its significance, except perhaps psychologically, and that the more it was used the less effect it had. Subject to further discussion at this meeting, he would be inclined to favor holding free reserves in the $400-$500 million range.

Mr. Leedy reported that the Tenth District was seeing evidence of the cumulative effects of recession. Employment was down but not as sharply as for the country generally, apparently because the district was less industrialized than most others. Department store sales had failed to match last year. Agricultural conditions continued good. Livestock in the district was up from a year ago, and the prices for meat animals were favorable. Business loans had decreased less since the first of the year than they did last year, while deposits stayed at about the same volume as last year.

As to policy, it seemed to Mr. Leedy that the target for free reserves should be pretty much in line with what it had been since the reduction of reserve requirements. The action taken in reducing reserve requirements produced publicity to the effect that $500 million of reserves were being released and, therefore, it should not appear that the level of free reserves was being reduced. Conditions reported at this meeting would seem to justify working toward the upper edge of that range of free reserves. As to the discount rate, Mr. Leedy felt that a reduction of not less than a half per cent should be made as quickly as feasible. Anything less would cause disappointment and undermine the psychological value of a reduction. The System had followed short-term market rates up when they were increasing and there was the same reason to follow them down, along with the matter of getting to a level of rates consistent with the System's purposes. As to the directive, Mr. Leedy agreed with the views expressed by Mr. Allen. The present wording of clause (b) indicated a rear guard action and that would be his objection to the wording suggested by Mr. Hayes. In his opinion, the directive should indicate that the System was taking the offensive, and wording such as Mr. Allen had suggested would seem appropriate. His own suggestion would be "to stimulate recovery in the economy."

Mr. Leach said that weaknesses in the Fifth District economy appeared to have deepened and spread further during February, with no evidence as yet of a leveling off in the decline. District production of bituminous coal dropped sharply in early February, continuing its decline over the past several months, and the most recent figures confirmed earlier reports of further cutbacks in textile operations. Insured unemployment continued to increase, and somewhat more rapidly than in the country as a whole. Average weekly hours in manufacturing industries in both durable and non-durable goods had dropped, cigarette manufacturing being a fairly important exception. Changes in business loans at district reporting member banks confirmed other evidences of weakness.

For some time, Mr. Leach said, he had been favoring somewhat greater reserve availability, but the recent reduction in reserve requirements created more than he had advocated. He had concurred in a $400 to $500 million free reserves range after the reserve requirement reduction because free reserves had been averaging around $250 million and it seemed to him that if the reserve requirement reduction were to have economic significance the System would have to leave outstanding a reasonable proportion of the reserves made available by the reduction. The $400 to $500 million range still seemed appropriate as a benchmark of desired ease. Mr. Leach went on to say that, in a declining economy flexible monetary policy requires the System to provide reserve ease appropriate to that situation. Fears of future inflationary dangers, serious as they may be, should not deter the System from fulfilling present obligations but rather make us hope that we will have the wisdom and foresight to tighten adequately as soon as there is an end to the need for this degree of ease. He saw no reason to tighten at this time, and recent rates in the short-term market made it clear that further ease would serve no useful purpose. The discount rate was not very significant at the moment but it was out of line with short-term market rates and with policy actions recently taken by the System. He thought that a reduction had been discounted and would have little effect on market rates, but it might have some effect on bank rates and it would give more room to increase later. He would much prefer a half per cent reduction to a quarter and felt that the reduction should be made around the middle of this month. He also felt that recent changes in the economy called for a change in the directive. Use of the expression "combatting economic recession" in clause (b) might be desirable.

Mr. Vardaman directed attention to the psychological aspect of the current situation. He sensed a spirit of apprehension in many banking quarters which seemed to be spreading rapidly. Some bankers appeared to be discouraging their customers from the normal amount of borrowing, and there was a disturbing parallel between the attitude of bankers now and in the early 1930's. He suggested that the Presidents of the Reserve Banks endeavor to point out to bankers in their respective districts that there was no basic change in the soundness of the economy as a whole and that consideration be given to working along the same lines through the bank examination function.

On the basis of the psychological factors, Mr. Vardaman expressed the view that a reduction in the discount rate might be interpreted as fear on the part of the System. If a change were made, he would much rather nibble at the rate and reduce it by only 1/4 of one per cent. At some time soon a further reduction of one per cent in reserve requirements might be considered, but for the moment the Reserve Banks and the member banks ought to emphasize the availability of loanable funds. As to the range of free reserves, probably the Committee ought to continue to set a goal in the area of $400-$500 million. On the directive, Mr. Hayes' suggestion would be acceptable. Instead of using the word "recovery" it might be better to use something like "restoring the economy to its normal level of activity." He doubted whether we had reached the point where use of "recovery" was necessary.

Mr. Mills suggested that in setting near-term System policy, it would be advisable to think back over observations Mr. Rouse made earlier in the meeting regarding the subject of plentiful reserves in the hands of the commercial banks as contrasted to congestion in the capital markets. Mr. Mills said further that this situation made it clear to him that reserves cannot serve as a substitute for savings of the kind that are essential for financing the capital markets and that, therefore, the risk of a sloppy market would be run if reserves were supplied too liberally in any attempt to relieve capital market congestion. In his opinion such a risk could be incurred if the System should supply reserves so aggressively as to bring them rapidly up to a positive $500 million free reserve level. He noted that on the basis of projections for the next three weeks or so and following the March 10 payment date for the Treasury's current offering, positive free reserves might range in the $375 million area, which range, as he saw it, would be acceptable as offering the commercial banks a freedom of maneuver in loaning and investment without the hindrance of a sloppy market. Subsequently, when long-term interest rates in the capital market sectors had adjusted to the Treasury offering and it was clear that additional reserves would be helpful to the economy, it might then be desirable to bring the supply of positive free reserves up to the $500 million level. However, Mr. Mills said that he would hesitate to supply new reserves in quantity until a long look could be taken at the impact of the Treasury's financing on the capital market. He thought that by that time, which might be ten days or two weeks hence, a discount rate reduction of 1/2 of 1 per cent would be in order to bring the discount rate into better alignment with market rates. He would favor a change in the wording of the directive with a preference for language of the kind suggested by Mr. Hayes.

Mr. Shepardson said that he regarded as significant the statement made by Mr. Young to the effect that continuing liquidation of inventories must inevitably bring stocks to a level from which they would again tend to build up, accompanied by a pickup in orders.

As to prices, there were indications that whenever an adjustment of prices took place, there was a response on the part of consumers, thus indicating that there was still a need for price adjustment. We were facing wage negotiations that Mr. Shepardson felt should take place in a framework of continuing restraint on price advances. There was no indication of any lack of funds to meet loan demands, he said, and it seemed to him that the present target of free reserves was ample. He would prefer to lean a little toward the low side of the range rather than to the high side, but the range itself appeared to be adequate. The discount rate seemed to be out of line but he did not see any purpose in making a quick change. The System had made a number of policy changes in fairly rapid succession, and he hoped that action on the discount rate might be deferred for some little time. At such time as a change was made, he saw merit in a shift of 1/2 of 1 per cent because he doubted the advisability of changing the rate too frequently in the current economic framework. He would have no objection to a change in the directive, but at this stage he would not like to shift to wording which indicated too strongly aggressive upward action.

Mr. Fulton said that the Fourth District, a highly industrialized area, was probably feeling the impact of the current recession more than most other areas. Steel production was at a low rate--one company reported operations the lowest since 1938. Automobile and appliance concerns were cutting back deliveries because of lack of sales, and no improvement was in sight. Oil companies simply were not buying and were shifting the supply of pipe back and forth among themselves. However, customers' inventories were generally in good shape except for automobiles and pipe. Steel warehouses were not overstocked and there was a fairly good mixture of inventories. The ore situation mentioned by Mr. Deming was definitely going to affect operations this year, for a great amount of ore had been brought down last year and stockpiles were ample throughout the Fourth District. One slight gleam of hope in the picture was the fact that representatives of machine tool manufacturers recently reported orders stronger than last year, and a large foundry reported a surprising number of inquiries about quotations for the fourth quarter of 1958 and the first quarter of 1959. Department store sales in February were about 10 per cent under last year and automobile sales were down about 25 per cent. Unemployment was up more than seasonally in January and up still further in February. Mr. Young had expressed the consensus of businessmen in the Fourth District, Mr. Fulton said, in suggesting that the current recession had the possibility of being deeper and longer-lasting than other recent recessions.

Mr. Fulton felt that if the discount rate were at or near 2 per cent the System would be in a better position to move in either direction. The rate should be reduced to that area as soon as possible, he said, and a reduction of 1/4 of one per cent would be niggardly in the face of existing market rates. A banker had remarked to him that the present congestion in the long-term market might be caused to some extent by comments that the recession was a very temporary thing; therefore, investors were not willing to put out money for long-term securities at existing rates, believing they could get higher returns if they waited. This banker claimed that the amount of savings was adequate for the supply of capital issues but that these issues were going begging because of anticipation of a revival. Mr. Fulton regarded $400-$500 million as an acceptable level of free reserves, preferring $500 million. In concluding, he expressed the view that the current recession was of great significance and not a temporary thing. He would change the directive in a way to indicate that the Committee was actively taking action to combat the recession.

Mr. Bopp reported that economic conditions in the Third District continued to deteriorate. Although data for the entire district could be interpreted to mean that it had a well-balanced economy, there had been areas of chronic unemployment for years, including the hard coal areas, like Scranton, Wilkes-Barre, and to a lesser extent, Pottsville; the old railroad repair area of Altoona; and on a seasonal basis, vacation areas like Atlantic City. Even a year ago, unemployment in all of these areas except Altoona exceeded 10 per cent of the labor force. It now exceeded 15 per cent in all except Altoona and had passed 20 per cent in Atlantic City. In January, unemployment in the fourteen principal labor markets of the district, seasonally adjusted, was 8.5 per cent of the labor force, compared with 6.7 per cent for the country as a whole. Only four areas were below the national average and none was as low as 5 per cent. The classification of three areas had been lowered and the district had seven areas of substantial labor surplus. Both new and continued claims for unemployment benefits, despite temporary aberrations, continued far above the levels of a year ago.

In another major area of System concern, namely, prices, Mr. Bopp reported that the cost of living in Philadelphia rose .1 of 1 per cent in January, compared with a rise of .6 per cent nationally. There seemed to be little if any upward thrust to consumer prices coming from strong demand. Some declines should be in prospect, encouraged by the change in pricing policies of some durable consumer goods manufacturers. In retail trade, new car registrations in January were 16 per cent below those of a year ago in Eastern Pennsylvania; in Philadelphia, registrations during the first three weeks of February were 25 per cent below a year ago. Department store sales collapsed as a result of the bad weather and disrupted transportation. For the year to date they were 7 per cent below a year ago; for the four weeks ending February 22, they were 12 per cent below; and for the last single week 39 per cent below. There had been little change in bank credit during the past three weeks. Business loans continued to be repaid and were now about 5 per cent below a year ago. The only optimistic note was a report on the expectations of the 400 largest industrial customers of the Pennsylvania Power and Light Company, the consensus being summarized in the phrases: "The downturn is about over, the upturn will come by summer."

Mr. Bopp expressed the view that these developments called for a policy of continued and possibly greater ease. As to the discount rate, it seemed to him the question was not whether it should be reduced, but when and by how much. As to timing, he felt it should be as soon as an "even keel" policy was no longer required for the current Treasury financing. In the light of the recent reduction in reserve requirements and the structure of market rates, and since this would be another move toward greater ease, he thought that period would be shorter than usual or than if we were moving toward greater tightness. He would, however, accept the judgment of the market specialist as to timing. As to amount, he thought the choice was not between 1/4 per cent and 1/2 per cent but between 1/2 per cent and some larger amount. In the light of market rates, one might justify a reduction of 3/4 per cent to a level of 2 per cent--the rate prevailing for a short time in 1955, when the boom was gaining momentum. On the other hand, he appreciated that only once had the System reduced the rate by more than 1/2 per cent and that was just after the stock market crash of 1929. For this reason, he would favor a reduction of 1/2 per cent at this time. In this connection he noted that the Philadelphia Bank's board of directors would meet this Thursday and that the next scheduled meeting would be two weeks from that date. As to the directive, Mr. Bopp said he would like to see it changed to convey the general idea that the Committee's purpose was to promote recovery by maintaining ease in the money market.

Mr. Bryan said he would like to report that the Sixth District was prosperous and doing well but that he could not make such a statement since the district's scorecard was continuing to show declines in practically all lines of activity. Private advices indicated additional plant layoffs and plant closings. District banks seemed to be responding in general fairly well to the current situation with regard to funds, and loans were up slightly over the same period last year. However, he sensed, like Mr. Vardaman, that the banks were policing their loans rather more carefully now than when the System wanted them to police loans strictly during a period of upturn. As the downturn continued, he felt that there might develop a tendency in the banking system toward more liquidity so that psychological reserve requirements could go a good deal higher than legal requirements.

On policy, Mr. Bryan expressed himself as pleased with the recent reduction of reserve requirements because it seemed to him that such action was necessary on all grounds. If he interpreted the statistics correctly, this meant that if the $500 million of reserves released by this action were kept available for the rest of this half of the year there would be a growth of total reserves slightly in excess of 3 per cent. He felt that the System should avoid doing anything through open market operations to offset that growth factor in a period of recession. Putting this in terms of free reserves, he would agree with a range of $400-$500 million, with the qualification that any error should be toward the top of that range or above it rather than toward the low side. Technically, a reduction in the discount rate was called for, but there was also the psychological problem which he found it difficult to appraise. A reduction of 1/4 of one per cent would give the impression of nibbling at the rate and he doubted whether this was an advisable posture for the System to take. As to the directive, he thought that it should be changed.

Mr. Johns said that some of his colleagues thought they saw indications that the rate of recession in the Eighth District was not as rapid as it had been. However, in his own judgment, the points leading to that view were not conclusive and other developments caused him to believe that the situation in the district gave no cause for cheer. For example, operations of the St. Joseph Lead Company had been shut down for 30 days; although there had been recent evidence of recalling employees to appliance plants, there had now been an announcement of a closedown of the General Electric Appliance Park in Louisville. Lumbering was not doing well, railroads simply were not buying,and last year's cotton crop was of deplorable quality.

As to policy, Mr. Johns said that he found himself in agreement with Mr. Leedy. He would not only urge working toward the upper end of a $400-$500 million range of free reserves, but he would favor setting $500 million as the operating minimum and not worry if the figure went somewhat higher. He agreed that the discount rate ought to be reduced, and as promptly as possible, whatever that might mean in view of the current Treasury financing. In his opinion the rate should not be higher than 2 per cent. Historically, this would be strong medicine but he felt that the patient needed strong medicine and he would not hesitate to administer it. In this connection, he suggested that it would be a good time for the System to exhibit some appearance of unity with respect to discount rate action. The directors of a number of the Banks were to meet the second Thursday of the month and it would be his hope that as many Banks as possible would act to reduce the rate at that time. The effective date of the change could be deferred if the Board regarded this as following too closely upon the Treasury financing. As to the directive, he felt that it was time to stop talking about mitigating recessionary tendencies and he would suggest, like Mr. Allen, that the wording of the directive be in positive rather than negative terms.

In a further comment, Mr. Johns said that he was becoming progressively more concerned about statements both within and outside the System to the effect that the discount rate was not very important or significant and that a change in the rate therefore was not significant. Even if the rate were reduced as much as one per cent there might not be a flood of discounting, Mr. Johns said, but this did not mean that a rate change was not important or without significance. To say that the discount rate was not an important or effective instrument of monetary policy was, in his opinion, to do the country a long-run disservice. It seemed important to him not to say by way of the rate that the degree of ease which had been achieved might not be here to stay, and he thought that this was the message that the System was conveying when the rate was not in line with short-term market rates. Mr. Johns recalled that a few years ago there was a thorough study of the discount rate mechanism which resulted in a revision of Regulation A, Advances and Discounts by Federal Reserve Banks. At that time it was stated that this would be followed up by a study of discount rate policy but the second study had never been made. He thought that no time was more appropriate than the present to launch that study, in order to decide what this implement of monetary policy was worth and how it should be used.

Mr. Szymczak said that he was impressed by the tone of pessimism--perhaps it should be referred to as realism--which dominated the comments at this meeting. He believed that the discount rate should be reduced to 2 per cent and that open market operations should be conducted with a view to having a level of free reserves of $500 million or a little more. He would favor a change in the directive along the lines suggested by Mr. Hayes.

Mr. Balderston said that he was somewhat concerned about the situation in the capital markets referred to by Mr. Mills, especially in the light of the profit squeeze that seemed to be affecting business planning. However, the immediate problem was the one to which Mr. Deming had referred, namely, rising unemployment. This meant that the System continued to be confronted with the dilemma of rising unemployment while prices remained sticky. The price situation was encouraging buyer resistance and prolonging price-cost maladjustments that needed to be removed if the economy was to regain its health. In the face of that dilemma, Mr. Balderston said he would favor a target of $400-$500 million of free reserves, and he would suggest a change in the directive using the positive approach mentioned by Mr. Allen. He would like some wording which would bring back into the directive the word "ease" and specifically would like to suggest that clause (b) provide that operations for the System Account be directed toward "encouraging sound recovery and employment by a policy of ease." As to the discount rate, Mr. Balderston would favor a change of at least 1/2 of 1 per cent when the Treasury financing was completed. If it were not for apprehension about the psychological reaction, he would favor a move to 2 per cent, but he noted that of the 27 downward adjustments in the rate since 1920 all but one of them had been in the amount of 1/2 of 1 per cent or less. In the event of a greater reduction, he was apprehensive that the press would carry the news in terms of this being the greatest reduction since 1929.

Chairman Martin said he thought the question of the amount of change that might be appropriate in the discount rate was one that was open to debate. He would not want to take a strong position himself. A 2 per cent rate was justified in terms of money market relationships, but certainly the psychological point was a very real one and the reduction could be misinterpreted. He agreed that it would be desirable to try not to have a sloppy operation, and he added that it might not be helpful in this particular situation to have the discount rates of the various Banks at different levels. With respect to changing the Committee's directive, he thought it was a question of a positive or negative approach and he had no strong views on that point. He would have no objection to the use of language such as "combatting recession and establishing conditions for recovery." The Chairman then presented different suggestions for changing the wording of the directive, including one that suggested language for clause (b) which would state that open market policy would be with a view, among other things, "to contributing further by monetary ease to resumption of stable growth of the economy."

The other members of the Committee indicated that they would favor such language.

Chairman Martin then said that the consensus of the meeting appeared to favor a range of $400-$500 million as a target for free reserves, with a leaning toward the higher end of that range rather than to the lower end.

There followed a general discussion of the discount rate level and procedure in the light of the views expressed at this meeting, at the conclusion of which Chairman Martin suggested that the matter be allowed to take its course at the respective Federal Reserve Banks.

In view of current circumstances, including the action taken by the Congress to increase the national debt limit from $275 to $280 billion, Mr. Rouse suggested eliminating from the directive paragraph (3) authorizing the sale direct to the Treasury from the System Open Market Account for gold certificates of such amounts of Treasury securities maturing within one year as might be necessary from time to time for the accommodation of the Treasury up to an aggregate of $500 million face amount.

> 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 contributing further by monetary ease to resumption of stable growth of the economy, and (c) to the practical administration of the Account; provided that the aggregate amount of securities held in the System Account (including commitments for the purchase or sale of securities for the Account) at the close of this date, other than special short-term certificates of indebtedness purchased from time to time for the temporary accommodation of the Treasury, shall not be increased or decreased by more than $1 billion;

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

The meeting recessed at this point and reconvened at 2:00 p.m. with the following in attendance:

PRESENT: Mr. Martin, Chairman
Mr. Hayes, Vice Chairman
Mr. Balderston
Mr. Fulton
Mr. Irons
Mr. Leach
Mr. Mangels
Mr. Mills
Mr. Shepardson
Mr. Szymczak
Mr. Vardaman

Messrs. Allen, Deming, Erickson, and Johns, Alternate Members of the Federal Open Market Committee

Messrs. Bopp, Bryan, and Leedy, Presidents of the Federal Reserve Banks of Philadelphia, Atlanta, and Kansas City, respectively

Mr. Riefler, Secretary
Mr. Thomas, Economist
Mr. Roelse, Associate Economist
Mr. Rouse, Manager, System Open Market Account

At this session there was a discussion of the study that had been made by the Special Committee appointed at the meeting on January 28, 1957 consisting of Messrs. Martin, Hayes, Allen, Balderston, Erickson, and Szymczak. In accordance with the agreement at the meeting on March 5, 1957, this Special Committee had been reviewing all of the operating procedures that had been presented in the report of the Ad Hoc Subcommittee as discussed at the meeting on March 4 and 5, 1953, with the exception of the matters relating to the housekeeping aspects of that Subcommittee's report. In the course of the discussion, there was presented for the approval of the Committee the following continuing operating policy that had last been reaffirmed at the meeting on March 5, 1957:

> a. It is not now the policy of the Committee to support any pattern of prices and yields in the Government securities market, and intervention in the Government securities market is solely to effectuate the objectives of monetary and credit policy (including correction of disorderly markets).

> Upon motion duly made and seconded, and by unanimous vote, the foregoing statement of policy was reaffirmed.

There was also presented for the consideration of the Committee the following continuing operating policy which, by unanimous action, was reaffirmed at the meeting of the Committee on March 5, 1957, pending completion and submission of a report by a Special Committee appointed at the meeting on January 28, 1957.

> b. Operations for the System Account in the open market, other than repurchase agreements, shall be confined to short-term securities (except in the correction of disorderly markets), and during a period of Treasury financing there shall be no purchases of (1) maturing issues for which an exchange is being offered, (2) when-issued securities, or (3) outstanding issues of comparable maturities to those being offered for exchange; these policies to be followed until such time as they may be superseded or modified by further action of the Federal Open Market Committee.

During a discussion of this statement of policy, Mr. Hayes said that, in an effort to promote general agreement, he would vote to approve the statement if it included the qualifying phrase, "as a general rule," after the word "shall" in the second line and after the word "shall" in the fourth line.

> A motion to reaffirm the statement in its existing form was approved, Messrs. Martin, Balderston, Fulton, Irons, Leach, Mangels, Mills, Shepardson, Szymczak, and Vardaman voting "yes," and Mr. Hayes voting "no."

> Messrs. Allen, Bopp, Bryan, Deming, Erickson, Leedy, and Johns stated that, had they been members of the Committee, they would have voted to reaffirm the foregoing statement of policy.

The following continuing operating policy was then presented for the consideration of the Committee:

> c. Transactions for the System Account in the open market shall be entered into solely for the purpose of

providing or absorbing reserves (except in the correction of disorderly markets), and shall not include offsetting purchases and sales of securities for the purpose of altering the maturity pattern of the System's portfolio; such policy to be followed until such time as it may be superseded or modified by further action of the Federal Open Market Committee.

Mr. Hayes stated that he would vote to reaffirm this statement of policy if the statement were amended to read as follows:

Transactions for the System Account in the open market shall be entered into ~~solely~~ PRIMARILY for the purpose of providing or absorbing reserves (except in the correction of disorderly markets), and shall, AS A GENERAL RULE, not include offsetting purchases and sales of securities for the purpose of altering the maturity pattern of the System's portfolio; such policy to be followed until such time as it may be superseded or modified by further action of the Federal Open Market Committee.

The Chair put a motion to reaffirm the statement in its existing form without the changes suggested by Mr. Hayes, and this motion was carried, Messrs. Martin, Balderston, Fulton, Irons, Leach, Mangels, Mills, Spehardson, Szymczak, and Vardaman voting to approve, and Mr. Hayes voting "no."

Messrs. Allen, Bryan, Deming, Erickson, Johns, and Leedy indicated that, had they been members of the Committee, they would have voted to reaffirm the existing statement of policy.

Mr. Bopp stated that, had he been a member of the Committee, he would not have voted to reaffirm the existing statement of policy but that he would have voted to approve a statement that was changed to read as follows:

"Transactions for the System Account in the open market shall, as a general rule, not include offsetting purchases and sales of securities for the purpose of altering the maturity pattern of the System's portfolio; such policy to be followed until such time as it may be superseded or modified by further action of the Federal Open Market Committee."

Mr. Hayes stated that he would be willing to vote for a statement such as Mr. Bopp had indicated he would approve.

It was agreed that the next meeting of the Federal Open Market Committee would be held on Tuesday, March 25, 1958, at 10:00 a.m.

Thereupon the meeting adjourned.

Winfield W. Riefler
Secretary