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, February 9, 1960, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Hayes, Vice Chairman
Mr. Allen
Mr. Balderston
Mr. Erickson
Mr. Johns
Mr. King
Mr. Mills
Mr. Robertson
Mr. Shepardson
Mr. Szymczak
Mr. Leedy, Alternate for Mr. Deming 1/

Messrs. Bopp, Bryan, and Fulton, Alternate Members of the Federal Open Market Committee

Messrs. Irons and Mangels, Presidents of the Federal Reserve Banks of Dallas and San Francisco, respectively

Mr. Young, Secretary
Mr. Sherman, Assistant Secretary
Mr. Kenyon, Assistant Secretary
Mr. Hackley, General Counsel
Mr. Thomas, Economist
Messrs. Jones, Marget, Mitchell, Noyes, and Roosa, Associate Economists
Mr. Rouse, Manager, System Open Market Account

Mr. Molony, Assistant to the Board of Governors
Mr. Koch, Adviser, Division of Research and Statistics, Board of Governors
Mr. Keir, Chief, Government Finance Section, Division of Research and Statistics, Board of Governors
Mr. Knipe, Consultant to the Chairman, Board of Governors

1/ Entered the meeting at point indicated in minutes.

Messrs. Eastburn, Hostetler, Tow, and Einzig, Vice Presidents of the Federal Reserve Banks of Philadelphia, Cleveland, Kansas City, and San Francisco, respectively
Mr. Coldwell, Director of Research, Federal Reserve Bank of Dallas
Mr. Stone, Manager, Securities Department, Federal Reserve Bank of New York
Mr. Brandt, Economist, Federal Reserve Bank of Atlanta
Mr. Litterer, Business Economist, Federal Reserve Bank of Minneapolis

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the Federal Open Market Committee held on January 26, 1960, were approved.

On February 1, 1960, the eleven available members of the Federal Open Market Committee approved a modification of the action taken at the Committee meeting on January 26, 1960, regarding the exchange of System Open Market Account holdings of approximately $5,507 million of Treasury certificates of indebtedness maturing on February 15, 1960. The modified action authorized exchange of the maturing securities into 4-7/8 per cent Treasury notes of November 1964 in the amount of $2 billion and exchange of the remainder (approximately $3,507 million) into 4-7/8 per cent one-year certificates.

The action taken by the Federal Open Market Committee on February 1, 1960, was ratified by unanimous vote.

Before this meeting there had been distributed to the members of the Committee a report of open market operations covering the period January 26 through February 3, 1960, and a supplementary report covering the period of February 4 through February 8, 1960. Copies of both reports have been placed in the files of the Committee.

Supplementing the written reports, Mr. Rouse made substantially the following comments on developments since the preceding Committee meeting:

> The volume of open market operations since the last meeting of the Federal Open Market Committee has been relatively small. The mopping up of the seasonal reflux of reserves after the first of the year has been accomplished and little needed to be done to keep the money market on an even keel during the Treasury's February refunding. A small amount of repurchase agreements was made against the "rights" at the close of the refunding as dealer holdings of the maturing issues rose to substantial proportions. The money market was generally tight throughout the period although at times there developed a little ease at the central reserve city banks in New York.
>
> The outcome of the Treasury refunding was very satisfactory as the attrition is relatively low and the public exchange for the four-year nine-month note is about what the market had come to expect. The result will substantially improve the Treasury's cash position over the next few weeks and will obviate any need for further borrowing until April, with a smaller amount of cash to be borrowed at that time. At the close last night the new 4-7/8 per cent certificates were quoted at 100-10/32, and the notes at 100-14/32, 22/32 above the issue price.
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> Since the last meeting the Government securities market has been quite strong, fortunately for the Treasury's financing operation, and rates have declined markedly. Scarcity of Treasury bills produced continuously lower rates, especially yesterday when most outstanding issues dropped about 30 basis points in the absence of any appreciable supply. The average rate in the auction yesterday was 3.563 per cent for 91-day bills, and 4.094 per cent for 182-day bills.
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> I want to mention also that the recent increase in the British discount rate and the subsequent increase in their bill rate at first gave a yield advantage to British bills over our Treasury bills of 3/8 per cent, which by

yesterday had increased to 5/8 per cent. The amount of funds lost from our market because of this differential is uncertain; probably not much so far, but the potential may be large.

Prices of notes and bonds also have improved sharply, with yields generally moving to new lower areas. As compared with earlier rates, which were above 5 per cent on a number of issues, the highest rate now available in the Government list is around 4.75 per cent for the new "when-issued" 4-7/8 per cent notes of November 1964; rates on other outstanding issues are considerably lower. Rate declines have occurred in commercial and finance paper and bankers' acceptances. The stock market has declined sharply.

All of these developments reflect doubts concerning the prospects for business and the implications for credit policy. The important question facing the market at this point is whether this apparent shift in psychology has substance and whether the present trend of interest rates can be sustained in the weeks to come. The market finds it difficult to reconcile the situation in the securities market with the degree of restraint being exerted on bank reserves.

Thereupon, upon motion duly made and seconded, and by unanimous vote, the open market transactions during the period January 26 through February 8, 1960, were approved, ratified, and confirmed.

During the course of Mr. Rouse's comments, Mr. Leedy joined the meeting.

Supplementing the staff memorandum distributed under date of February 5, 1960, Mr. Noyes made the following statement with regard to economic developments:

In his <u>Reserve Banks and the Money Market</u>, Randolph Burgess observed 30 years ago that with the establishment of the Federal Reserve System seasonal swings in interest rates had been almost eliminated. In the seasonal factors he calculated for the period 1914 to 1932, which ranged from a low of about -3 per cent in July to a high of +4 per cent in October, there was very little change from December to January. This was in contrast to a sharp year-end break shown for the 1894 to 1914 period, when the December factor was +8 per cent, and January -4 per cent.

In recent years it appears that some of the seasonality of rates around year-end may have returned. Despite the general upward trend, in eight out of the last ten years the bill rate declined from the end of December to the end of January, and we hear frequent reference in the market to the year-end peak and the January decline.

There also seems to be a seasonal pattern emerging in appraisals of the economic outlook, although it evades exact measurement. To what extent the bearish reappraisal of economic prospects that is currently spreading so rapidly in the press and financial markets reflects only the usual transitory seasonal disillusionment, and to what extent it is based on more fundamental changes in the economic situation is difficult to judge. In part, at least, the answer must be found in the expectations that came before. The observers who saw a strong surge of activity in early 1960 were the ones who had the firmest expectation of rising prices and speculative inventory accumulation piled on top of the normal rebuilding that was generally anticipated.

While it is sometimes overemphasized, the manufacture and sale of automobiles must play an important part in any analysis of the business situation. Recollections of 1955 played an important role in the thinking of those who saw a swelling boom in 1960. Dealer sales of 455,000 new cars in January were certainly a real disappointment to these analysts, and a comfort to those who had expressed some skepticism when the prices of the 1960 models were announced last fall.

The low level of new corporate financing in January and the limited schedule of offerings for this month suggest to some that business plant and equipment expenditures in 1960 may not exceed the intentions expressed in late 1959 by as large a margin as they have exceeded early intentions in other boom years. Loan demand at commercial banks has also disappointed those with great expectations. Whether it has declined more than seasonally is hard to say, but it certainly has not shown the contraseasonal vigor that would bear out expectations of an inflationary boom.

If developments so far in 1960 have been disquieting to those who saw a run-away boom around the corner, they have also provided little comfort to the disciples of doom. All of the aggregative measures of the output of the economy are showing gains up to or exceeding informed earlier estimates. GNP is still expected to be close to $500 billion for the first quarter. As more fragments of data become available, advance estimates of the index of industrial production have been revised up rather than down and we are currently thinking in terms of 170. Employment appears to have been well maintained. Seasonally adjusted department store sales held about the same level in January as December, which is all the more impressive on the heels of a record-smashing Christmas season.

Construction activity again confounded the experts by inching up to a seasonally adjusted annual rate of $54.9 billion, the highest January on record.

The shakeout in the stock market has unquestionably both reflected and raised doubts as to the future. Whether the appearance of high first-quarter profits, taken together with somewhat lower yields on fixed-income securities, will stem the tide of profit-taking remains to be seen.

In summary, it appears that this winter the usual seasonal declines have had more than the usual seasonal effect on expectations, due primarily to the exceedingly bullish attitude that prevailed around the year-end. Investors and speculators are adjusting to a less buoyant outlook than seemed certain a month or so ago. At the same time, consumers and businesses remain confident and are producing and spending at record rates for this time of the year. The prospects for avoiding an inflationary boom are certainly brighter--and as is inevitably the case, the possibility that we may be confronted with a major readjustment is similarly enhanced. Taken altogether, however, it is hard to see how the tempering of enthusiasm that has taken place in the last few weeks can be anything but beneficial, regardless of what lies ahead.

Mr. Thomas presented the following statement with respect to financial developments:

Evidence of the anticipated poststrike boom has not as yet appeared. While it is clear that economic activity is at a generally satisfactory level, there are few, if any, signs of undue fervor. This is particularly true in the financial area.

Following extremely tight conditions in the money market with sharply rising interest rates and an unusually heavy seasonal loan demand during December, money has eased notably in January. Interest rates declined and bank loans were reduced about as much as they had increased in December. Figures now available as to the sharp increase in business inventories during December may help to explain some of the heavy loan demand in that month. It seems hardly likely, however, that the loan decline in January reflects a corresponding cut in inventories. The decrease in business loans was no greater than usual for January, but there was a larger than usual decline in loans to finance companies and a substantial drop in security loans. Partial figures for the first week of February show a moderate upturn in business loans, which is not usual for that week.

In addition to the decrease in loans, banks also continued to liquidate Government securities in January, with the largest decrease in the one- to five-year maturity group. As a result total loans and investments at city banks declined more in the five weeks ending February 3 than in the same period of any other recent year in total dollar amount and also relative to the December increase.

New corporate security issues continued relatively light in January and are expected to be even smaller in February. New issues by States and local governments, on the other hand, increased considerably in January, but a smaller volume is on the calendar for February. Stock prices, after rising close to the 1959 high at the close of December, declined sharply in January, and with yesterday's sharp drop are close to the low of the past 12 months. During that period the various indexes of averages have generally fluctuated within a range of about 10 per cent. At present levels of prices, even if allowance is made for higher earnings this year, yields on principal stocks are still very low relative to bond yields, although somewhat above recent lows. There continues to be a growing feeling among investors that some shifting of portfolios from stocks to bonds is wise.

In contrast to stocks, bonds have risen in price since the first of the year and yields on long-term Government bonds are back to November levels. Yields on outstanding high-grade corporate bonds, however, have continued close to the highs which they reached in December. Long-term Government bond yields have not declined as much as those on shorter-term securities. Yields on 3- to 5-year Government securities, which have generally been higher than those on other maturity categories, have declined to around the lowest levels of last October. Yields on Treasury bills are at the lowest levels since late August.

Under the circumstances, Treasury financing operations have been eminently successful, with low attrition and a substantial exchange for the four-year, nine-month note, as well as for the certificate. These issues are now selling at premiums. The Treasury will evidently not need to do any more financing until the end of March or early April.

The easier money situation is clearly a result of action by the market itself, rather than of monetary policy. Since mid-December, Federal Reserve holdings of Government securities have been reduced by more than $1.5 billion, offsetting reserves supplied largely by the return flow of currency and by System payments to the Treasury. Required reserves have declined by at least the usual seasonal amount. Net borrowed reserves of member banks have continued generally at around $400 million.

The decrease in loans and investments at city banks has been accompanied by a greater than usual drop in deposits--both demand and time--at those banks. At country banks during the first two weeks of January, deposits increased somewhat more than they did in the same period last year; loans declined seasonally, but holdings of Governments increased. Figures are not yet available for country banks as of the end of January, nor are we yet obtaining weekly deposit figures for country banks from all the Reserve Banks.

It is estimated that the total money supply, seasonally adjusted, may have declined slightly in January after increasing in December. These computations are based on new improved seasonal adjustment factors. The total is only about half a billion dollars--or less than 1/2 of one per cent--larger than a year ago. The trend of the money supply has been slightly downward since midsummer--after rising for a year and a half. The current figure is a little over $5 billion larger than the peak of mid-1957--an average annual rate of increase of less than 2 per cent. Turnover of deposits at banks outside financial centers has risen at a faster pace; in the last quarter of 1959, it was over 6 per cent above the figure for a year earlier and about 7 per cent above the 1957 peak. The combined figures of money supply and turnover indicate a rate of growth in total monetary transactions of nearly 4 per cent a year since mid-1957.

Question may be raised as to what extent increased turnover of cash balances can be relied upon to finance further growth in economic activity, without some increase in amount of deposits. Liquidity--in the form of short-term assets other than cash--has expanded greatly in the past two years, but its active use may call for some additions to the supply of cash or at least the availability of cash. Perhaps the time has come when some further growth in bank credit and in the money supply should be permitted. In the absence of strong pressures for credit expansion--a situation that seems to exist at present--it would appear safe to provide some additional reserves and thereby add to the availability of credit without the risk of unduly encouraging excessive credit commitments.

Mr. Marget commented substantially as follows with regard to the United States balance of payments:

When I reported to this Committee on January 12, the figures for transfers of gold and dollars to foreigners for the month of December were still incomplete. Now that we have the complete figures, we can step back a bit and take a look at the figures for the whole of the calendar year 1959, as compared, in particular, with the figures for the calendar year 1958.

It was in the year 1958, as you will recall, that we had the massive outflow of gold which was the occasion of such widespread discussion in the press, so much of it so mistaken in its emphasis on an alleged "flight from the dollar." As we emphasized at the time, there was no "flight from the dollar" in 1958. The proof of this was that at the very time this "flight" was supposed to be taking place, foreigners were actually increasing their holdings of dollar balances in the United States by over $1 billion. By the same token, there was anything but a "flight from the dollar" in 1959. On the contrary, the increase in dollar balances held by foreigners was more than twice as large in 1959 as in 1958. Indeed, the actual gold outflow in 1959 was also less than half of the gold outflow in 1958. It can fairly be said, therefore, that in 1959 the foreign holders of dollar balances, instead of running away from the dollar, gave the dollar an even stronger vote of confidence than they had given it in 1958.

These foreign holders of dollar balances are not irrational. In giving this vote of confidence they were, quite obviously, expressing a judgment that the United States would succeed in its efforts to meet the problem of which the visible symptom was the combined figure for gold outflow and additions to dollar balances held by foreigners, namely, the problem of the over-all deficit in the balance of payments of the United States. What do the final figures for 1959 show in this respect?

If we were to deal only with the totals for 1958 and 1959, one might wonder what there was in these figures to give anybody, foreigner or other, any basis for confidence that the problem was likely to be solved. The figure for 1959 is $3.7 billion, as against a figure of $3.4 billion for 1958, the year in which the world was suddenly made aware that the United States did in fact have a balance of payments problem of serious dimensions. But of course the explanation of the paradox is to be found in the movements of gold and dollars, and therefore our over-all balance of payments, within the calendar year 1959. The early months of the year, instead of showing a reversal of the deterioration in our balance of payments which had occurred in 1958, showed an intensification of the deterioration, to the point that, as I reported to this Committee, the projections made by the Balance of Payments Group of the National Foreign Trade Council suggested that we should be lucky if we ended 1959 with an over-all deficit no greater than $4.5 billion, as compared with the $3.4 billion of 1958. The fact that we ended with an over-all deficit much closer to the 1958 figure than had been supposed possible on the basis of the showing in the earlier months of 1959 is a measure of the degree of improvement that we in fact had in our over-all balance of payments in the later months of the year.

But, as you have been made aware by these reports of mine at roughly three-week intervals, that improvement has not been of a kind that left us in no doubt whatever as to the future pace and solidity of the adjustment that seemed to be taking place. I had occasion last time, for example, to report the relatively poor export figures for November, and to suggest that, while an explanation for this poor showing might be found in the steel shortages growing out of the strike, the figures themselves provided a warning against supposing that all our troubles with the balance of payments were behind us for good and all. It is gratifying to report that the trade figures for December are very much better than the November figures; and the preliminary gold and dollar figures for January of this year are also distinctly encouraging. There is no reason to discount good news when it comes, particularly since the news is of developments of the kind that have been eagerly awaited, not least by those foreign holders of dollar balances who, according to our gold and dollar figures, gave the dollar, and therefore the monetary authorities of the United States, an even stronger vote of confidence in 1959 than they had given in 1958. The essential point is that the basis of this confidence is the belief that balance of payments developments depend, to a very large extent, upon the policies pursued by the monetary and fiscal authorities of the country experiencing the balance of payments difficulties. In the present instance, that means a belief that the fiscal and monetary authorities, in determining their actions, are not likely to confuse evidence that a salutary process of adjustment is under way with a conclusion that the adjustment has been virtually completed.

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

Data becoming available in the past two weeks indicate that business has continued to move forward at a very satisfactory pace, as Mr. Noyes has already told us. On the other hand, the growing public impression that an inflationary boom may be avoided, widely commented on at the last meeting, seems to be equally evident today and seems to find considerable justification in recent business and credit statistics. Doubtless the persistent stock market decline has had good psychological effects, as has increasing awareness of the prospective Federal Government surplus. The failure of automobile sales to keep pace with production schedules is another factor. For this and other reasons there may be some modest drop in steel output in the second quarter.

I believe it would be a mistake, however, to overemphasize these moderate tendencies, since the basic outlook for production, employment, and spending is strong, and the possibility of an inflationary boom cannot be dismissed completely while the year is yet so young. It is worthy of note that residential construction, which was one of the major laggard elements in the economy, has taken a turn for the better; and exports will probably provide somewhat greater stimulus to the economy than in the past year.

In general, bank credit developments in January were about in line with the seasonal pattern, in contrast with earlier expectations of highly exuberant demands. Continuing ample cash earnings of nonfinancial corporations, coupled with relief from December seasonal pressures, and relatively conservative investment outlays by such corporations, help to explain their active buying of securities which, together with buying by public funds and other nonbank investors, has been a major cause of the substantial decline in market interest rates. The downward rate movement may also reflect a normal reaction to earlier excesses in the other direction. These better market conditions were doubtless in large part responsible for the successful market borrowings which enabled the finance companies to make unusually heavy repayments of their bank loans in January. Security loans and bank investments were also off sharply last month. Nevertheless, the nation's banks remained in a tight position, with liquidity ratios especially low in the New York banks, to whom large corporate borrowers look as a major source of term loan financing as well as of current seasonal credit. The New York banks now appear to be making a strenuous effort to prevent a further large rise in their loan-deposit ratios, and this will of course have a bearing on their attitude toward an increase in the prime rate over the next month or two.

The outstanding success of the Treasury's refunding operation should confirm earlier hopes that the Treasury could remain out of the market until early April. Hence, we can consider the latter part of February and most of March as constituting a so-called "free period" for monetary policy.

For the time being, I can see no reason to change our basic policy of credit restraint. As I have said before, I would hope to see somewhat greater growth in the money supply in the current year, and I was interested in the comments of Mr. Thomas along that same line, but there is no great urgency in meeting this problem as long as business is going ahead so satisfactorily and credit demands seem about in line with the normal seasonal pattern. We have been giving careful study in the New York Bank to Mr. Bryan's proposals for a more objective quantitative approach to open market operations. A number of questions have arisen, many of which have apparently also troubled Mr. Thomas. While we are inclined to agree generally with the reservations expressed in his letter of February 4 to Mr. Bryan, we also feel that continuing analysis of what is happening to total reserves should be of real help to the Committee in formulating its judgments, and to the Manager in carrying them out. We certainly think that this whole area deserves further study.

Meanwhile, I think we should preserve the status quo with respect to open market pressure as measured by the general feel of the market, with no hard and fast target of net borrowed reserves and with the usual ample leeway for the Manager to take account of developing pressures or their absence.

As for the discount rate, the case for near-term action has been much weakened by the sharp decline in short-term market rates and the calmer business appraisals occurring since we decided to defer rate consideration pending completion of the Treasury refunding. From a Treasury standpoint we would be free to move before our next meeting; but whereas a few weeks ago I would have expected that action in late February would be desirable, I no longer think so. I think we shall have ample opportunity to review the matter in March, by which time we shall have a better basis for knowing whether the present lull in economic pressures is of lasting significance or a mere passing phase of a developing boom. At present business and credit conditions do not justify a discount rate rise. If we did move, it would doubtless bring a rise in the prime rate, whereas the banks may hold off action if we stand pat--and I see no reason for the System to want to set off a wave of rate increases in the next few weeks. Inaction on our part would have the further advantage of allaying the fears of those who see an international "rate war" developing--although I would not urge this as a significant factor if the domestic scene called for a discount rate increase at present.

The directive may, I think, be appropriately left unchanged.

I should like to report very briefly at this time on the progress of the new program for the collection of statistics on the Government securities market approved at the FOMC meeting of January 12.

We held a meeting with senior representatives of all the dealer firms on January 29, introducing Miss McWhinney to them and outlining the scope of the program. Mr. Young

> and Mr. Mayo participated in this meeting. Since that time Miss McWhinney, in association with representatives of both the Board and the Treasury, has met individually with representatives of each of the dealer firms. Although the response has been varied, no dealer has indicated a refusal to comply, and several have warmly endorsed the entire program. Each of the dealers now has copies of all the proposed schedules, and the technicians in each of the firms are now studying the detailed problems concerned with actual reporting. After taking into account suggestions that the various firms may offer, aimed at improving methods of obtaining the data we intend to collect, final schedules will be prepared for clearance with the Bureau of the Budget. We hope to reach this stage by mid-March. I think it is barely possible that full scale operations on the new basis may begin in April, although the recital of difficulties that we have heard from some dealers (including the need they face to employ and train additional clerical staff) may persuade us to begin somewhat later.

Mr. Johns said that basically he did not see that business conditions or prospects for future activity had changed much over the past few weeks. In his opinion, the situation still called for efforts in the direction of doing what monetary policy could do about resisting pressures that make for price increases. Thus far in 1960, and in late 1959, open market operations appeared to have brought about appropriate firmness in monetary restraint. Total bank reserves, seasonally adjusted, did not seem to have increased, and it did not appear that the money supply, seasonally adjusted, had risen. He would suggest that open market operations in the near future be conducted with a view toward holding the money supply and bank reserves, seasonally adjusted, about level; if the money supply or bank reserves should increase in the near future, he hoped the rise would be slight. Within the framework of a stable, or nearly stable, money supply and total reserves for the next few weeks, short-term interest rates and net borrowed reserves might increase if demands for money should become stronger. This, he thought, should be no cause for alarm. On the other hand, if such demands did not materialize, decreases in net borrowed reserves and money market interest rates would not disturb him.

With respect to the discount rate, Mr. Johns commented that an argument could be made for an increase of 1/2 per cent, and he would not go so far as to say that the argument was footless. Except for interest rate developments in the past two weeks or so, which some believed to be unusual and transitory, the discount rate had been below its "normal" relationship to other money market rates. Other countries had marked up their rates recently, and it could be argued that if the System did not do likewise this might be conducive to deterioration of the long-run terms of trade. On the other hand, since the cause of the recent interest rate decline was not altogether clear, it seemed probable that a discount rate increase at this time would be taken as an announcement of a change in policy toward significantly greater restraint, and he did not believe that such greater tightness should be the aim or intent of System policy at this time. Therefore, he concluded that an increase in the discount rate would be inappropriate at this time. Neither would he favor a change in the policy directive.

Mr. Bryan commented substantially as follows:

The latest figures for the Sixth District seem to show generally continuing strength in the economic situation. They do not, as noted at our last meeting, show in many of the figures a differentially greater strength than the nation as a whole: a matter of note to us because we have come in the postwar period to think that comparatively greater gains in the District's economy are typical.

Figures available since our last meeting indicate no change in nonfarm employment; a very minor increase in manufacturing employment; a decrease in department store sales; a serious decrease in construction contract awards but an increase in construction employment; and an increase in commercial bank loans that contrasts sharply with a decrease for the nation.

In connection with nonfarm employment we have shown a decrease in Florida, Mississippi, and Tennessee, which is notable because Florida has for the entire postwar period been the outstandingly strong spot in the economy of the Sixth District.

As we see the picture nationally, the situation is one of great current strength and probable but not certain further strength for some months. The rather dramatic price improvement that has recently occurred in almost the whole range of fixed income maturities raises inescapable questions. It is tempting on the one hand to assume that these changes are purely temporary, seasonal, and technical in character. It is almost equally tempting to argue, from the magnitude and consistency of the changes, that they arise out of some more fundamental shift in the economic and monetary climate. In our judgment, it is still much too early to say certainly whether the recent reduction in yields is temporary and seasonal or represents a more fundamental shift in the economic and credit tide. We thus conclude that at this time it would be perilous to rest our policy on either assumption.

In the light of this situation it seems to me again reasonable to express the view that we should effect a reserve position of the banking system that does not permit an excessive expansion of credit and the development of an unsustainable and probably speculative boom. At the same time--because of the long period in which, in adjusting to a previous excessive easing of reserves, we allowed no growth of reserves at all--I continue to believe that we must now contemplate, until events indicate otherwise, a modest growth in the reserve supplies of the banking system.

For want of a better figure I continue to believe--a belief in which judgments can well differ--that for the time being a growth rate of 2 per cent annually in total reserves would keep the banking system under restraint but minimize the dangers implicit in an effort of an expanding economy to grow against a fixed reserve base arrived at either by policy or by inadvertence.

Accordingly, I would suggest that our daily average reserve target for February be $18,585 million with a range for practical administration of the Account of $18,635 to $18,535. Thus far, in February (as of the opening of business on Monday, February 8th) we have had daily average reserves of approximately $18,515 million. 1/

Mr. Bopp reported that business conditions in the Third District had continued to improve in recent weeks, with advances moderate but generally widespread. With the effects of the steel strike all but dissipated, the employment picture was brighter; in the four areas for which December reports were available, slightly over 5 per cent of the labor force was jobless compared with just under 7 per cent a year earlier. New unemployment claims had been declining seasonally and were below the levels of both 1959 and 1958. Department store sales had been registering increasingly large gains on a year-ago basis, and volume in the past four weeks was 7 per cent above the corresponding 1959 period. Sales of new cars in eastern Pennsylvania were low in December, primarily due to shortages. Steel production in the Philadelphia steel district had been running at or above theoretical capacity for 10 weeks; operations in the latest week were at 101 per cent of capacity, compared with

1/ Mr. Bryan subsequently furnished a table, attached at the end of these minutes as Item No. 1, providing information on the derivation of these figures.

94 per cent nationally. Freight carloadings continued high above year-ago levels, while construction contract awards in December registered an increase of 11 per cent over the year, as against a 3 per cent decline nationally.

Mr. Bopp said that business loans of district weekly reporting banks seemed to have declined somewhat less than seasonally since the turn of the year. In the past two weeks, investments had decreased as banks reduced their holdings of Governments. Adjusted demand deposits had continued downward, while time deposits had increased moderately. The basic reserve position of large city banks showed improvement in the past few weeks; the average basic deficiency declined from $73 million to $13 million. Borrowing from the Federal Reserve Bank had reflected this change by dropping from $65 million to $13 million. Country banks, on the other hand, had increased their borrowing from the Reserve Bank. As the result of these mixed changes, the Third District now accounted for 4 per cent of total borrowings from the System, as compared with 6.7 per cent and 8.8 per cent, respectively, in the preceding two weeks.

As to policy, Mr. Bopp expressed the view that this was a time for watchful waiting. He would not recommend any change at this time in the degree of restraint, the discount rate, or the directive.

Mr. Fulton stated that Fourth District activity continued at a high rate. Steel production was averaging about 97 per cent of capacity, with Cleveland and Cincinnati around 100 per cent. He was told, however, that there was a noticeable softening in the demand for steel and that the production level would decline. The forecast of production for the year 1960 had been reduced from 135 million tons to 125-127 million, but the reduced estimate was still considerably higher than the largest previous year, 117 million. Industry expected that operations for the year would average out at about 80 per cent of capacity, which was a desirable rate from the standpoint of the mills, and profits were expected to be quite good. Auto companies had cut back tonnage for the second quarter, and other users of steel were not stocking inventories as expected because they were getting whatever they needed when they needed it and also because they did not want to borrow to carry inventories. Some domestic users of foreign steel reportedly were willing to pay damages to get out of their contracts with foreign producers. The steel workers were still going strong and productivity was being maintained at the high rates of November and December.

Mr. Fulton said that machine tool companies reported new orders much higher than the fourth quarter rate and expected a good year from the standpoint of profits and production. Anticipating strong auto production, the rubber industry had produced tires in great volume and inventories were high. However, production had been cut back, shipments were now running ahead of production, and the industry expected a good year as a whole. Auto sales in the Fourth District had been quite good, higher than in recent years, but used-car sales were not so strong. A glass company supplying the auto industry had cut its estimate of automobile production to 6.8 million, while the rubber companies contended that a 6.4 million car year would be doing very well. It appeared that dealer inventories would amount to about one million cars by the end of this month, which would necessitate quite a drastic cut in production. The impact of the new compact cars had not yet been thoroughly appraised, but it was expected that stickiness in larger cars would to a degree be taken up by the smaller models. Reports from various metal-working industries indicated that they were expecting a good year in terms of stable production and satisfactory profits. Department store sales for the four weeks ended January 30 were 13 per cent above last year. A disturbing factor, however, was that unemployment trends had not kept pace with the improvement in business. A longer time would be necessary to appraise that development, but it did seem that a higher rate of unemployment was becoming something of a continuing factor. Reports were being heard in every quarter of price increases for finished goods. Prices had gone up 5 to 10 per cent for manufactured goods, particularly at those companies that signed up with workers in terms of the contract that the steel companies signed. Business loans in the district were just about even with December 30 figures, and the banks did not expect a large increase in those loans in the immediate future. They felt that the payment of corporate taxes in March would not be accompanied by unusual borrowing and that the using up of corporate liquidity would probably not come to light in terms of credit demand until April or May.

All in all, Mr. Fulton said, businessmen and bankers expected a good year. As Mr. Noyes had suggested, they felt that expectations for a booming economy after the first of the year were much too high, and that a leveling-off of those expectations was a healthy thing in terms of permitting a sustainable economy for a longer period.

Mr. Fulton felt that the Desk should continue about the same degree of pressure that had been brought to bear in the past few weeks, without easing. He also felt that neither the discount rate nor the directive should be changed at this time.

Mr. King said he found himself in agreement with practically everything that had been said thus far. He thought that this was not a time to take any positive action one way or the other, and that it was definitely a time when the Desk should not apply any more restraint. In his opinion, the apparent moderation of the course of the prospective boom was partly due to the experiences of many people during the last recession; they remembered the lessons learned during that recession quite well and were not going to get into a position where caution was thrown to the winds. A thing that seemed to be working in favor of the System and the economy at the present time was that people apparently were not going to permit themselves to get overextended. That had been the basis for his view, expressed several months ago, that there was not going to be a wild boom after settlement of the steel strike. He felt that people had learned their lessons and were not likely to forget them in a hurry.

Mr. Shepardson said he considered it fortunate that some of the excessive exuberance manifested a few weeks ago seemed dampened somewhat. He also considered it fortunate that basic indicators were still strong and suggested continued growth. Like two weeks ago, the situation seemed to be one calling for watchful waiting. During this seasonal period, it was difficult to predict just what would happen when spring opened up, and in the circumstances he would maintain the present position of restraint.

After commending Mr. Bryan for his work in trying to develop useful policy guidelines for the Committee, Mr. Robertson said that this was a time when, without a change in policy and without a change in the degree of restrictiveness that had been followed, the Committee found itself in a situation different from that prevailing when it adopted the existing policy directive. At that time inflationary credit expansion was going on, but today that could not be said. In his opinion, the directive should not be adopted under certain circumstances and then left intact under different circumstances. If the directive were changed, it was possible, of course, that the Committee might come back to it in a short time; his own thinking was on that side. However, in view of the situation existing today, he thought it would be desirable to change clause (b) of the directive to eliminate the reference to "restraining inflationary credit expansion." If this were done, clause (b) would provide for fostering sustainable economic growth and expanding employment opportunities. If the Committee wanted to add "without inflation," that would be agreeable to him. In either event, such a directive would be more indicative than the existing directive of the situation at the moment.

Mr. Robertson agreed with the view that there should be no easing or tightening. As Mr. Bopp had said, this was a time for watchful waiting.

Mr. Mills said he proposed to pick up at a point where Mr. Bryan had left off and urge that the Committee focus its attention on the kaleidoscopic fluctuations that had occurred in the prices of United States Government securities over the past six weeks or thereabouts, particularly the very sharp rise in prices that had taken place over the past two weeks with a consequent decline in yields. As he picked up the discussion today, there had been general acknowledgment that those movements were related to natural market factors. If such were the case, the Committee should be chary in embarking on any actions that would tend to alter the outlook that the market had taken on the movements in prices of United States Government securities. If the Committee did so, it would be flying in the face of the long-expounded concept that the Federal Reserve believed in a free Government securities market and that there should be a minimum of interference with the movements therein. This harked back to comments he had made at previous Committee meetings, and the January 26 meeting in particular, that the maintenance of a status quo position, if that were interpreted in the level of negative free reserves and if the Committee had in mind negative free reserves in the range of $500 million, would inevitably mean further pressure on the reserve positions of the banks and further restriction of the money supply. It seemed quite probable that the marked shrinkage of bank deposits in January was more than a seasonal symptom and was fundamentally a reflection of the pressure of a continually maintained level of negative free reserves. If that should be an objective of the Committee, he felt it would be damaging two ways. In the first place, it would completely destroy the outlook in the United States Government securities market that had been derived from a free market and was in his mind a reassuring factor. Second, it would put far greater pressure on the reserve positions of the banks than justified by the economic outlook, as depicted in the various comments today.

A great deal had been said, Mr. Mills noted, regarding the money supply and the fact that it could be held to a very low level of expansion or forced to contract below an earlier level, and that the economy would not suffer from that trend in that there was a make-up of the deficiency through increasing velocity in the turnover of money. However, it seemed quite possible that the velocity being thought of was the velocity of turnover of bank balances in the hands of large corporations or other personal or institutional entities whose balances are substantial. At the other end of the spectrum, he would suspect that there might be quite a different picture in the statistics of the smaller businessman or entrepreneur who, at his most affluent time, operates with only small balances and is dependent, by and large, on augmenting those balances through the use of credit. If there was any basis to that reasoning and if, as he understood, it is a purpose of the economist to look at the whole of consumption as the means of obtaining stability and growth in the economy, too much pressure, and unrelenting pressure, would sooner or later so push back the accessibility of credit to the large body of consumers in the smaller operating brackets that their ability to consume and refine the product of the country's manufacturing mechanism would be severely damaged.

Mr. Mills said that he would not favor changing the discount rate. He would be willing to accept Mr. Robertson's proposed wording of the directive in lieu of the language he (Mr. Mills) had offered on several occasions, although he still commended his suggestion to the consideration of the Committee.

Mr. Leedy reported that Tenth District conditions continued to show strength. The sharp advance in nonfarm employment late last year had brought the job level back to its pre-strike magnitude. Increased employment had occurred not only in plants directly affected by the steel strike and other strikes in the district, including some in the packing industry, but also in several nonmanufacturing areas, including trade and services. Department store sales were up in January, but not as much as the national average, the rise being only 2 per cent. The trend in business loans to which he referred at the preceding Committee meeting had continued. Contrary to the national pattern, the seasonal movement in these loans had been much less pronounced than in past years; loans to manufacturing and mining companies had actually increased contraseasonally, and loans to commodity dealers had also increased. There had been some decline in deposits at weekly reporting banks; with the current trend of loans and these losses of deposits, there had been some increase in borrowings by reserve city banks from the Reserve Bank.

As to policy for the forthcoming period, Mr. Leedy said it seemed to him there should be a continuation of what had been done in the past few weeks. The change that had occurred recently seemed to him pretty much in the psychological area. As pointed out, all of the major economic indicators were still on the side of strength. Although there were some indications of a possible slowing down, for example, in steel output and auto production, the over-all picture continued to be one of such strength that there seemed no sufficient reason for any basic change in System policy. He subscribed to the view that there should be some addition to the money supply, but to inject additional funds for that purpose at this time did not seem to him appropriate. The policy that the Committee had been following in recent weeks had permitted a general decline in interest rate levels, and nationally there had been at least a seasonal decline in business loans. Until the outlook was more clear and until there was a confirmation or some repudiation of the change in psychology that had occurred, it seemed to him the Committee should continue what it had been doing, making certain that the pressure on bank reserves was not increased.

Mr. Allen said the assumption that business activity would rise vigorously through the first half of the year was being tempered by more rapid inventory building than had been anticipated. Steel shortages were rapidly being eliminated, although some items, chiefly the lighter ones, were still in short supply. The auto industry is so important a user of steel that it receives preference, but if auto production should be cut back, steel supplies should ease substantially. Auto production in January was 690,000, and it did not appear that February would exceed that figure. Therefore, if original first-quarter production schedules of 2,250,000 cars were to be achieved, 900,000 would have to be produced in March, which seemed unlikely in the light of sales thus far. January sales were 455,000, better than in 1959 or 1958 but not as good as in 1957, 1956, or 1955. Inventories on January 31 were 794,000 units. If 700,000 cars were produced in February, then even if February sales exceeded those in January by 10 per cent, inventories on February 29 would be at the very high figure of 994,000. It seemed more certain every day that first-quarter production would be less by 150,000 to 250,000 than originally forecast, and that a 7 million car year was out of reach. The industry was re-evaluating its schedule mix. The increased sales of compact cars--22 per cent of the January total--were forcing conversion of more assembly lines to the small cars, and the feeling was growing in Detroit that this was a transition period in a permanent adjustment of models to less expensive automobiles. A check with producers of television sets and household appliances in the Chicago area indicated that sales of these items, like automobiles, had been less than anticipated, with the result that some involuntary inventory building was occurring. On the other hand, sales of nondurable goods continued strong in January. Daily average sales at department stores were 8 per cent above last year, compared with 7 per cent for the country. Also, the rise in orders for producers' capital goods had continued, and the prospects for farm income and home building, rather dim a few months back, had improved. Although sales of consumer durables were not as strong as exuberant forecasts had suggested, they were at relatively high levels and could increase further in the spring. The increased ease in the money market in recent weeks had not been reflected in the reserve positions of the Chicago banks to the extent that it had shown up elsewhere. The most important fact was the effect of loan changes. The large Chicago banks had not had the January decline in loans which was shown by the New York banks.

Summarizing, Mr. Allen said that business was at a very good level and inflationary expectations had diminished. He subscribed to the view of those who felt that the Committee should continue about as it had been in the matter of monetary restraint. He would favor no change in the discount rate and would prefer no change in the directive, perhaps being overly influenced by the Seventh District loan picture toward continued use of the word "inflationary" in the directive. He would not feel too strongly if the majority of the Committee wanted to adopt Mr. Robertson's suggestion, but his personal preference would be to leave the directive as it stood.

Mr. Mangels said that most recent changes noted in the Twelfth District were the result of seasonal factors. Lumber production and new orders had declined, but the mills had been operating at a little better than the usual rate for the past month or so. The lumber people were awaiting developments in the next 60 days to see how they would fare. Total construction contracts awarded in the district were up 3 per cent against a year ago, with increases in both residential and nonresidential construction, primarily in apartment house and motel type construction. An FHA survey indicated that about half of the building contractors in the district expected fewer starts in 1960 than in 1959, and it had been noted that there was a longer period between finishing and selling homes. Steel production in January declined, which was to be expected following the high rate of production in December to meet critical shortages. The three major producers were operating at 94, 87, and 77 per cent of capacity, respectively. It was expected that demand and prices would hold up through March, but that in the second quarter that there would be some reduction of sales in certain lines. Aluminum production had increased substantially with the addition of another potline by Alcoa. Two producers were operating at capacity and the other two at about 75 per cent of capacity. The increased demand reflected foreign buying and also new uses of aluminum. The copper strike had been settled by one company and two others were hopeful of a settlement within a week or ten days. While no recent over-all figures on automobile registrations were available, in California registrations for the second week in January increased 60 per cent from the first week. Department store sales in January were about 3 per cent over a year ago for the district as a whole, but in Seattle and Portland there was a decline. Bank loans in the two weeks ending January 27 showed a further decline of $130 million, and holdings of Government securities declined about

$180 million. Demand deposits were down almost $390 million, a larger decline than for the country as a whole, and time deposits were down $80 million, about half of the decline for the United States as a whole. The banks were still losing savings deposits to savings and loan associations paying 4-1/2 per cent dividends and to the Government securities market. There continued to be a large volume of small purchases of Government securities by individuals. To indicate the degree of tightness of the banks, in the past week reporting banks purchased Federal funds to the extent of about $1.5 billion, this being six times the amount of sales. This week they expected to buy $1.4 billion, with virtually no sales. Borrowings from the Reserve Bank had been somewhat on the heavy side, with over $100 million of loans outstanding on February 4. Borrowings were scattered and were not in large number, but those who borrowed tended to come in for substantial amounts.

As to policy, Mr. Mangels noted that the signal was still red as far as Treasury financing was concerned. Even if the light were green, however, he would be inclined to align himself with those who suggested holding the line. This would mean net borrowed reserves of somewhere around $400 million. At the January 13 meeting of the San Francisco directors, it appeared that the sentiment was moving toward an increase in the discount rate of either 1/2 per cent or 1 per cent, but last Thursday the directors came in convinced that no change should be made. Mr. Mangels felt that he would favor leaving the directive pretty much in its present form. By the time of the next Committee meeting, however, a change perhaps would be warranted.

Mr. Irons said there had not been any significant changes in the Eleventh District. Business activity was going along at a good level, department store trade was off less than seasonally in January, and the crude oil situation was satisfactory in terms of what it had been earlier. Employment and unemployment figures were satisfactory, with the changes in January less than seasonal. On the nonfinancial side, therefore, the general picture was one of slight to moderate improvement at a high level of activity. There seemed to be less thinking among businessmen and bankers as to the probability of a strong inflationary push than two or three months ago, but the optimism may have been dampened by factors that might change.

On the banking side, Mr. Irons said, there had been a bit more than the usual seasonal decline in loans. There had been a decline in investments and more than a seasonal decline in deposits, the bulk of the deposit decline having been in interbank deposits. The banks, principally the city banks, apparently had been under considerable pressure since the first of the year. Borrowings from the Reserve Bank in the past several weeks have been larger in amount and larger in proportion to total borrowing from the System than was earlier the case. They totaled about $130 million on one or two days, which was high for the district, and rather consistently had been running about 10 per cent or more of the national total. The borrowing was coming in large part, dollarwise, from four or five of the larger reserve city banks, but there had also been some increase in the number of "real" country banks that were borrowing. A few of the country banks that borrow seasonally had begun to borrow sooner than in other years.

The national picture, as Mr. Irons saw it, did not call for a change in any of the basic policies that the System had been following. He would not favor a change in the discount rate at this time. He would like to see open market operations continue about as they had been during the past two-week period, feeling that this represented the appropriate amount of pressure on reserve positions. He would prefer not to change the policy directive at this time, although he felt that the Committee might be getting nearer to the point where a change would be in order.

Mr. Erickson said that most of the statistical measures in the First District continued to show growth, but that the situation did not have any of the characteristics of a boom. A spot check of steel distributors, users, and warehousers last week indicated that inventories were regarded as back to normal and adequate except for certain specific shapes or sizes. During the past two weeks district banks had been sellers of Federal funds in a moderate way. They used the discount window on the average slightly more than in the previous two weeks, but borrowings since the first of the year had averaged only 2.5 per cent of the System total.

Mr. Erickson expressed agreement with the summarization of the current situation made by Mr. Noyes and said that he would continue present policy, making no change in the discount rate or the directive. Although he agreed that the language suggested by Mr. Robertson was more in line with the present situation than the existing directive, he would prefer to wait until the next Committee meeting before making a definite decision. He would favor giving the same instructions to the Desk as were given at the January 26 meeting.

Mr. Szymczak said that, as at the time of the January 26 meeting, he believed the System should provide reserves to the extent that the Account Manager could do so without disturbing the market, or putting it differently, the Account Manager should absorb less of the reserves provided from other sources. He felt there was a tendency to get wedded to certain net borrowed reserve figures, as we have done before, and that people in the System and outside the System knew this and acted accordingly, frequently with disturbing consequences in the money market and the Government securities market and, therefore, by the nature of the habit formed it was difficult to establish a change in policy when a change became evidently required. He felt it would be better for the System to vary the net borrowed reserve figure, whether on the basis suggested by Mr. Mills, or on the basis suggested by Mr. Bryan, or on the basis of the current seasonal situation; it seemed advisable to allow some of the reserves provided by outside influences not to be absorbed by selling securities. However, in his opinion the over-all economic picture was one of strength and, therefore, he would not suggest a change in the directive at this time or a change in the discount rate at this time.

Mr. Balderston stated that in view of his comment at the January 26 meeting that the Committee should not be deceived by the doldrums of February, what he proposed to suggest at this time might come as something of a shock. Continuing, he said that in pondering the fundamental questions Messrs. Mills and Bryan had raised, he had taken advantage of the experience and skills of Messrs. Thomas, Young, and Noyes and their colleagues in order to gear his own thinking. He found himself ready to join Messrs. Mills and Robertson in favoring a change in the language of the directive, primarily because he thought it was timely for the Committee to consider its responsibility in respect to the long-run money supply.

Mr. Balderston said it seemed to him the present period was a long moment of uncertainty. The Committee might be witnessing merely a reappraisal of expectations or a pause in the recovery, or it might possibly be witnessing the beginning of a downturn. It was his guess as of today that business might still be climbing, but at a decelerating rate, and that the economy might be starting a rolling adjustment that could persist for some time. The current recovery, he noted, would celebrate its second anniversary in May. What gave him cause for concern was not the dampening of bullish expectations, which might only reflect February pessimism. The Committee had warned itself two months ago that this might happen. What did impress him, however, was the behavior of the financial markets. The decline in loans and investments had been greater than was to be expected for seasonal reasons, and the calendar of corporate issues was small. While a surge of offers like that in March 1956 might still be experienced, he saw no evidence of that as yet. The money markets had eased on their own initiative, and this easing was reflected in the current decline of the bill rate.

It was time, Mr. Balderston suggested, for the Committee to ponder its policy, its directive, and its procedure. On the second and last of those steps, he had had the help of Messrs. Thomas and Young. His conclusion was that the directive should be modified to reflect the present uncertainty, the disappearance, whether temporary or not, of speculative ebullience, and the need for further growth in the money supply. He feared that the Committee would hang on too long to the restraint it had been exerting. The wording he would suggest for clause (b) was "to fostering sustainable growth in economic activity and employment while guarding against excessive credit expansion." Like the language Mr. Robertson had suggested, this directive would drop the word "inflationary." If the directive were changed in this manner, he would recommend that policy be implemented by adding about $20 million a week to the reserve base, after allowance for seasonal and other transitory factors, which would permit a rate of growth in the money supply of about 2 per cent a year.

At this point, there were distributed copies of a table of projected operations allowing for 2 per cent growth. The term "projected operations" represented operations necessary to allow for seasonal changes plus growth of currency in circulation and required reserves at an annual rate of 2 per cent, a total of $20 million a week. The figures were presented on a weekly basis and on a cumulative basis through the end of June.

Mr. Balderston then said that by using these calculations and following a procedure designed to implement such a policy the Committee would add about a half a billion dollars a year to the currency in circulation and about half a billion dollars a year to required reserves. Expressed in terms of percentages, the increase in currency would be about 1.6 per cent a year, and in required reserves a little less than 3 per cent a year. He hoped that this procedure, if it should seem desirable, would employ a language that would not expose the Committee to the criticisms from the outside that would surely be leveled at it if the Committee were to use a percentage figure like 2 per cent. He proposed, therefore, that the weekly increment be expressed in absolute terms, even in Committee discussions, so that the risk of misinterpretation might be minimized. Consequently, he suggested $20 million per week as expression of Committee policy.

His reason for urging this procedural change, Mr. Balderston said, was to foster continued growth at a high level. In 1958 the Committee added to the money supply by 4 per cent, and in 1959 by .5 per cent. The Committee, quite properly, let the economy grow up to the enlarged supply of reserves put into the market in 1958. However, one who pondered the admonitions of Messrs. Mills and Bryan might conclude--as he had--that the Committee should now begin again to provide for growth in the money supply at a steady pace. To fail to do so might magnify any decline in the economy, if and when it occurred.

Mr. Balderston said he had sought to explain the change in his own thinking and his concern regarding the impact that continuing restraint might have upon the long-run money supply unless the Committee shifted procedure. If it shifted procedure and adopted what Mr. Thomas had worked out, and there would be good reason, he felt, it seemed to him that it would be timely to change the directive as well.

Chairman Martin said the Committee was indebted to Messrs. Bryan and Balderston for doing work on a formula approach that might be of help. The Committee was also indebted for the points on the money supply that Mr. Mills had made over a period of time. He thought that all of the Committee members were beginning to recognize these points as meriting consideration.

The Chairman said he did not think the Committee was as far apart as might appear from the discussion. All appeared to be leaning in the same direction. The question came to a matter of judgment on what the economy was going to do, and with regard to that he felt there were varying judgments.

Turning to the directive, Chairman Martin said this involved a problem that had concerned him since the Open Market Committee started meeting at three-week intervals with all of the Presidents in attendance. If the Committee was going to meet so frequently, it must be prepared to take cognizance of minor shifts in the economy as well as major shifts, that is, the short-run as well as the longer-run problem. For that reason, Mr. Robertson's comment was pertinent. The dramatic shift in the past couple of weeks certainly was not indicative of inflationary psychology. Whether inflationary implications were still dominant was a matter of doubt, on which there could be differing judgments.

Chairman Martin said that he had tried hard over the past week end to pull together his own thinking. He came out, essentially, that he still was not persuaded that there had been a fundamental change in the economy. He did not believe, however, that the adjustment of the past several weeks was something that could be shrugged off. To say with certainty that this was just a minor adjustment in a long bull market (a bull market in a business sense) would be unwarranted. The Committee was not sure of the state of business even before the steel strike, and then the strike came into the picture. It was now settled, and a new assessment of business might be taking place. One way to think about the matter would be in terms of assuming the worst, that is, that the country was starting into a business recession. He did not assume this for a minute, but he put the possibility forward for the purpose of an intellectual exercise. Using such an assumption, the question was what the System should be doing; whether it should drastically revise the discount rate and push on the entire problem.

As he saw it, the Chairman continued, the System ought to be looking at the growth of the money supply and the factors that would produce it. It should be looking for some orderly growth in the economy on the assumption that the country was not in a serious downturn but was in a modest adjustment that would require picking up. This might be entirely different from 1957 and 1958 and might require an entirely different assessment of the picture. As things stood, it seemed to him that the Committee ought to give serious consideration to whether it should not adjust the directive mildly at this point. He did not feel that this was a matter of great importance. If the Committee adjusted the directive and a few weeks from now should find that the current movement was temporary, it could readjust the directive and reinstate the existing language if that seemed appropriate. At least, however, the Committee would be showing an awareness of what was occurring in the economy.

As to the money supply, Chairman Martin said it concerned him that in talking to some informed individuals in the past week or ten days, he found a number of them convinced that the System has been easing. They would have been much more alarmed had they known that the recent developments occurred without any easing of pressure by the Federal Reserve. This was a rather interesting point to him, the Chairman said. It indicated that the System would be tightening against a trend, and he questioned whether the Committee would want to do that. He felt that the situation had moved beyond the point where continuation of an even-keel policy on account of Treasury financing was called for. There was still the matter of the Treasury payment date, but he believed the Treasury was sufficiently over the hurdle so that this was not a serious consideration--at least, it was not a consideration serious enough to guide the extent to which the Committee might wish to mop up reserves coming into the market independently of Federal Reserve action.

The Chairman noted that the discussion today had been in terms of moderate growth of the money supply. For example, Mr. Balderston had suggested $20 million a week and Mr. Bryan about $31 million this month, and others had suggested supplying some reserves. His judgment was that the Committee should give serious consideration to whether, under present conditions, it wanted to maintain the status quo. If so, the Committee could be working actively against a current trend in the money market and exerting more pressure than current events warranted. There might be a tightening two or three weeks from now and the System might want to go in the opposite direction, but at present the Committee was dealing with the problem of the money flow.

Chairman Martin said he interpreted the consensus today as favoring no change in the policy directive, although a substantial minority favored a modest change. Personally he did not think a change in the directive of fundamental importance, but there had been some shifting, whether one called it psychological or anything else. If an outsider compared the discussion at the January 12 Committee meeting with the discussion today, he would probably say there was not much justification for having exactly the same directive on January 12 and February 9.

The Chairman then called for discussion of the consensus, specifically as to whether it would be wise to make a modest adjustment of the directive on the basis of what had happened between January 12 and February 9, and with full recognition that the Committee was going to meet again on March 1, at which time it might wind up by reinstating the present language.

Mr. Allen noted that the psychology in January reflected much more of a boom feeling than when the current directive was first adopted in May 1959. Committee members evidently felt quite different today than they did on January 12; most seemed to feel somewhat different. The country was not in a boom at present, but business was very good.

Upon request, the language for clause (b) of the directive proposed by Mr. Robertson and that proposed by Mr. Balderston was read.

Mr. Hayes then said that he leaned toward continuing the present directive for at least another three weeks in view of the fact that clearly the consensus favored keeping policy about the same. He had had the feeling that a change in the directive should suggest a measurable change in policy. It might well be that the time was getting near when the Committee would want to do that, but he did not feel that the majority favored a basic change in policy now. Therefore, the Committee might want to defer a change in the directive for another three weeks rather than to get whipsawed into a quick reversal if developments during that period indicated that the recent trends did not represent a very lasting economic change.

Mr. Hayes recalled that he had had sympathy for a long time with the thought of trying to let the money supply expand a little, and he still had that feeling. However, he believed there was nothing inherent in present policy or the present directive to preclude a change in the order of 2 per cent a year from occurring. From the standpoint of a short-term operational guide to the Desk, an instruction for this kind of an increase in the money supply would be almost meaningless. The Desk could hardly see $20 million a week in relation to the kind of factors that it was offsetting all the time and would scarcely be able to tell whether such an objective was being accomplished or not. Of course, the Account Manager could look later and see whether, in a general way, he had gotten toward that goal, but in day-to-day operations the Desk could not be guided by such an instruction. This did not mean that a $20 million increase could not be built into the projections. He rather liked the idea of setting the projections up cumulatively, as Mr. Thomas had done, with allowance for growth; to a very minor degree, the Committee would be giving recognition to the desirability of having this growth. However, the swings are such that the Manager could not determine whether he would accomplish that growth or not within any three-week period.

Mr. Rouse said that he thought Mr. Hayes had stated the problem precisely.

Mr. Young said it was not the feeling of Mr. Thomas or himself that the Desk could turn the situation around in a three-week period from an actual decline in the money supply to no growth to a little bit of growth. The Committee might have to play along with this procedure for several months before there was evidence that it was taking hold.

Mr. Szymczak said he felt there might be good reason for changing the directive more frequently than had been done in the past, but he doubted whether this was the time to make such a decision. In the first place, although he might be wrong, he felt that recent developments were seasonal. Second, the time to make a decision to change the directive more frequently would logically seem to be at the annual organizational meeting on March 1. At that time it could be decided whether, in the event of a determinable change in the situation, even if it were only slight, the Committee would want to change the directive. However, to change now, and then come back again to the directive that had been outstanding for a long time, might create confusion both for the Committee and the reader of the Committee's policy record. To summarize, he felt that the recent economic and financial developments were of a seasonal character, he felt that any decision to change the policy directive more frequently than in the past should be deferred until the March 1 meeting, and he would favor providing some reserves within the terms of the present directive because he believed there should be some easing and also because he would like to get away from a fixed level of around $500 million net negative reserves. To remain at a fixed net negative reserve level too long, he said, made it more difficult to change when the time came to change.

Chairman Martin withdrew from the meeting at this point to receive a telephone call.

Vice Chairman Hayes indicated that he hesitated to go forward with the meeting in the Chairman's absence because there seemed to be some difference in his views and those of the Chairman with regard to the directive.

Mr. Mills then suggested taking a poll of the Committee members with regard to the directive and with regard to whether additional reserves should be supplied, either according to one of the formulas that had been suggested or otherwise.

Chairman Martin then returned to the room.

In response to a suggestion made while the Chairman was out of the room and of which he was advised after he returned, Mr. Thomas undertook a technical explanation of the proposal of Mr. Balderston. He said the differences that existed between this proposal and the total reserve guide suggested by Mr. Bryan were in some respects significant. Ignoring for the moment the smallness of the figures, whichever guide was used, and the question of how good the instruction might be to the Desk from the standpoint of day-to-day operations, from a procedural standpoint this was an approach that said buy or sell so many securities regardless of what happened to net borrowed reserves or total reserves. Adjustments might be necessary because of variations in market factors from projections. The proposal would produce the same results as the use of total reserves or net borrowed reserves if growth in the economy proceeded according to the pattern indicated on the table and if, therefore, borrowings remained unchanged. However, if the growth in the money supply should be greater than projected, it would be necessary for the banks to meet their additional reserve needs by borrowing, which would mean that total reserves would increase by the amount of the borrowing; net borrowed reserves would increase and banks would be under greater restraint, as they should be. If the growth was less than projected, the banks could pay off their borrowings and be under less restraint. Under the total reserve formula, if the growth was greater than considered desirable and the System attempted to keep the supply of reserves stable, the Account would have to sell in the market to offset borrowings, and that would make the banks discount more or force them to liquidate securities. If the System tried to buy in the market to offset borrowings, that would create more ease. Under the Balderston proposal, if growth of currency in circulation and required reserves were as projected, reserves would increase as desired and net borrowed reserves would not change. If growth were greater than projected, however, total reserves would increase, but so would net borrowed reserves, thus putting additional pressure on the market. If growth were less than projected, borrowings would be permitted to decline, and total reserves would decline. Under the net borrowed reserve standard, any greater growth than projected would be supported by open market operations. This would be different from the total reserve standard, under which the System would try to offset any changes in reserves due to changes in borrowings. Under the Balderston proposal, if there was a tendency toward more growth than projected, restraint would rise because borrowings would have to increase. If growth were less than projected, restraint would decrease because borrowings would decline. The figures given in the Balderston proposal would allow for about a half billion dollar annual increase in currency in circulation. This would include not just the currency included in the money supply but also bank vault cash; and in a sense it would allow for growth in the reserves of nonmember banks held in the form of vault cash. The action permitting member banks to count some vault cash as reserves meant that the formula would have a little less effect than formerly. One would have to make less allowance for that factor than formerly. If it was desired to effect a 2 per cent increase per year in the money supply, that would call for adding about $8 million of reserves a week--corresponding to the $30 million a month figure in Mr. Bryan's proposal. The Committee could vary the directive by saying that the Desk could take care of currency in circulation and then have $8 or $10 million left for growth in total reserves.

Mr. Johns inquired whether the projections related to the Balderston proposal made allowance for seasonal changes or for intramonthly fluctuations in float, and Mr. Thomas replied in the affirmative.

Mr. Hayes then asked whether the Balderston proposal would not be a better guide for what the Committee might want to do over a period of several weeks than in a particular week. He repeated his belief that an instruction in accordance with this proposal would not constitute an adequate guide for a week's operations without some additional guidance, such as to keep the degree of pressure about as it had been or a little stronger or a little weaker.

Mr. Johns suggested that the study would be incomplete unless the Committee reconsidered carefully the necessity of offsetting short-run, self-correcting fluctuations in the reserve supply, for example, intramonthly fluctuations of float. That factor alone would complicate the figures substantially and make for wide fluctuations in a short period of time. If there was no offsetting, it was his view that nothing dire would happen.

Chairman Martin indicated that he thought Mr. Johns had made a valid point.

Mr. Hayes then commented that he found the Balderston proposal interesting and deserving of thought. However, if it was being considered as a basis for changing the type of operating guidance given to the Desk, he felt that such a step should be deferred until there had been an opportunity to study the matter further. In other words, while it was an interesting proposal, he did not feel that the Committee should adopt it today.

Chairman Martin agreed, stating that the proposal should be put in the same category as Mr. Bryan's suggestion of two weeks ago.

The Chairman then said that the real problem this morning was whether there was any way of finding words to cover the type of situation that existed at present. To judge by the discussions at this meeting and the January 26 meeting, there was more concern within the System than for a long time about the question of growth of the money supply and when to do something about it. Mr. Rouse had said that the market was generally tight during the past two weeks. However, the rate structure was not tight. Therefore, the problem got into terms of the feel, color, and tone of the market.

Mr. Hayes suggested that the Desk might be instructed to continue about the same degree of pressure, bearing in mind, however, the wish of the Committee that, within the general framework of present policy, some modest increase in the money supply could be encouraged.

At this point Mr. Mills again proposed that the Committee members be polled on the directive and the manner in which reserves should be withheld or supplied during the period until the next Committee meeting.

Chairman Martin said he had no objection, although the shades of difference were so slight that he was not sure a poll would reveal too much. There might be a go-around on the directive, and then discussion of the implementation of the directive, for there would appear to be different questions of implementation depending on whether the directive was renewed or changed. At least that was the way he sensed the discussion this morning.

The Chairman then suggested going around the table for views on the directive.

Mr. Johns said he found it rather difficult to comment on the directive unless he knew the majority determination concerning policy, for the directive ought to express what the current policy was. If he must comment, however, he would adhere to his position that he would mildly prefer not to change the directive now.

Chairman Martin suggested that it was important to have in mind what was involved. The Committee was talking about modest degrees. The problem was one of restraint or less restraint, but not ease, and it is always difficult to handle such a problem in terms of words.

Mr. Bryan noted that he was not presently a member of the Committee. He then said that he had not come to the meeting with a change in the directive in mind. However, the arguments made by Messrs. Robertson, Mills, and Balderston were profound. He believed that he would favor a change in the directive, and either form of wording that had been proposed for clause (b) would be satisfactory to him.

Mr. Bopp said he agreed with Mr. Bryan.

Mr. Fulton said he would go along with that view also, with preference for the language suggested by Mr. Balderston.

Mr. King expressed doubt as to whether a change in the directive would accomplish anything substantial and suggested that the instruction to the Desk was more important. He felt the Committee had reached a point where it was going to have to abandon net borrowed reserves as a guideline to the extent that it had used that figure heretofore. His thinking would be to avoid any additional tightness and, if necessary, to increase the Account portfolio by whatever amount was necessary to avoid additional tightness. This did not mean necessarily that some securities might not be sold on any given date, but he would lean against divesting securities from the portfolio on balance even if net borrowed reserves went to any particular figure. Instead, he would prefer, so to speak, to turn the market loose. If the Committee was likely to turn around in three or six weeks, he questioned whether any directive that might be given the New York Bank would be much more meaningful than the existing directive. In substance, he would not change the directive at this time, but he would let the level of net borrowed reserves go to whatever point it might go as long as it did not get out of the present general range. He would, on balance, not be a seller of securities.

Mr. Shepardson said that although he had not proposed a change in the directive, the discussion had brought out arguments for making a change. He would favor Mr. Balderston's suggestion.

Mr. Robertson said that he would favor a change in the directive.

Mr. Mills said he also would favor a change and that he would prefer the wording suggested by Mr. Balderston to the language suggested by Mr. Robertson.

Mr. Leedy said he was troubled by the fact that in the past the Committee had changed the directive only when it made a change in policy. In his own thinking, he was not yet prepared to make a distinct change in policy. While the Committee should be thinking about some additions to the money supply, it seemed to him that this was not the time to add to the money supply affirmatively. On the other hand, he would not like to see any further tightening occur in reserve positions. In his opinion, the directive, as it read, could remain in effect indefinitely. The Committee was always desirous of restraining inflationary credit expansion, even though at the present time it was not confronted with actually doing that. The Committee would be fighting windmills if it attempted to restrain inflationary credit at the moment, but in theory it was always seeking to do that. His preference would be to wait until the next Committee meeting before deciding to embark actively on any program that involved an actual change in policy.

Mr. Allen said he would prefer not to change policy or change the directive at this meeting.

Mr. Mangels said he had thought originally that the Committee might wait until March 1, but he would not object to changing the directive now. He would not increase restraint in the forthcoming period; instead, he would be inclined toward a lessening of restraint.

Mr. Irons said that the question was one of using a broad, continuing directive that would change two or three times a year or a short-term directive that might change from meeting to meeting specifically to fit the situation at the particular time. In thinking of the proposal to change the directive today to provide for fostering sustainable economic growth and expanding employment opportunities, he did not see what could happen to warrant changing such a directive three weeks from now or even in a longer period, for the Committee always would want to do such things. However, if the Committee was going to change the directive today, in a period of uncertainty, with the possibility of changing again in three weeks, he felt the Committee ought to spell out in detail what it proposed to do for the next three weeks and what might cause it to change again. The directives that had been suggested could go on indefinitely for he could not conceive when the Committee would not want to foster sustainable growth and employment opportunities. In his judgment, what was needed now, rather than such a change in the directive, was careful study and thought as to how to develop a form of specific directive that might be changeable in two or three or six weeks, in contrast to broad generalities. On the basis of that reasoning, he would not change the directive today.

Continuing, Mr. Irons said that he would have no objection to a little ease in the market. He had felt that way at the past two meetings. He would try to maintain about the degree of restraint that had existed recently, but he would go on the side of ease if the market situation seemed to call for that. This was not too good as a guide to the Desk, but it seemed better than a mechanistic formula calling for the Desk to put in $20 million a week. He was yet not ready to accept such a formula and felt that it should have more testing, because he did not think the Manager of the Account had the slightest idea what the situation was going to be in the market next Thursday. The Manager of the Account could sense an attitude in the consensus of Committee thinking, but he (Mr. Irons) would not want to use a mechanistic approach, whether in terms of total reserves, net borrowed reserves, or anything else.

Mr. Erickson said he agreed with Messrs. Leedy and Allen. He would not change the directive at this time. Also, he found it difficult to find a way of going ahead in terms of supplying reserves at so much a week. For the next three weeks, if there were any errors he would make them on the side of ease.

Mr. Hayes said that he found himself closely in agreement with the views expressed by Messrs. Leedy, Irons, and Erickson. Although the Committee should study the general question of what it meant the directive to do, the Committee thus far had been following the practice of setting forth in the directive a kind of basic approach to what monetary policy should be. Thus, the directive had normally been changed only two or three times a year. He did not feel that circumstances today warranted one of those changes. Perhaps the situation would warrant such a change by the date of the next meeting, at which time the Committee could vote to change the directive and consider what kind of directive should be issued.

Mr. Hayes repeated that he would favor continuing about the same degree of pressure, with the Desk mindful of the discussion about the money supply, which would suggest veering on the side of ease in a minor way. He felt strongly that a purely mechanistic directive would not be workable because the Manager of the Account has to deal with five or six different elements, such as the psychology of the market, the feeling of the banks, or actual reserve changes, all of which might call for some market action that could not possibly be predicted.

Mr. Szymczak repeated his earlier suggestion that the Committee consider at the March organization meeting whether the directive should be changed whenever the Committee makes slight changes in policy in the direction of either restraint or ease. Up to the present time, he noted, the Committee had not followed the practice of reflecting slight policy variations in the directive. If the practice was going to be changed, that should be decided at the annual meeting and the directive then changed more frequently. As yet, he was not ready to accept the refinements that had been suggested, but he might be if he studied the matter more and action was taken at the next meeting. Thus, while he would favor somewhat less restraint in the period ahead, he did not favor enough change in policy to change the directive at this time.

Mr. Balderston said that he would favor changing the directive today.

Chairman Martin said that he too would favor a change, but that the consensus appeared to be against it. In his opinion, however, this was not the most important thing. The important thing was that even those who did not favor a change in the directive leaned toward slightly less restraint. He was glad that the question of the form of the directives had been raised and discussed. The annual meeting was coming up, and perhaps there should be a further discussion of that point. However, he noted, the matter of finding language to express degrees of restraint is difficult. The Committee did not have a mechanistic approach, and he agreed with that completely, but it was necessary to have some guidelines.

Mr. Balderston said that what had been most helpful to him was the point referred to by Chairman Martin in his comments that there is a distinction between ease appearing in the market due to the operation of factors that the System can not control, restrain, or push and ease or restraint that is created through System open market actions. The question was whether, in the next three weeks, the Committee would want the Desk to mop up any ease that just happened to appear in the market. It seemed to him that that was the crux of any instruction given to the Desk.

Mr. Shepardson said he thought this was essentially the same thing that Mr. Johns had been getting at in his comments. It would mean not trying to pick up what might be called inadvertent ease. It was essentially the same idea that he (Mr. Shepardson) had attempted to express at the January 26 meeting. It would mean letting such inadvertent changes as might come from the action of the market develop. The Desk would not try to mop up excess reserves that might come into the market because of factors other than System operations.

Mr. Hayes commented that the Desk had been following a policy of not automatically offsetting everything that happened in the market. If an attempt had been made to offset fully the tendencies toward ease generated by the market itself, net borrowed reserves might have been a billion dollars or more, and even then such tendencies might not have been fully offset. The Desk was not guided by the single thought that it must offset what happened in the market itself. This was merely one of several elements that the Desk must be watching.

Mr. Shepardson then commented that to the extent the Committee aimed at a fixed target of net borrowed reserves, say $500 million, it would automatically tighten the situation by continuing to mop up reserves as they appeared. On the other side, there was the situation that existed in the spring of 1958 when the System was aiming at a certain level of free reserves and kept pouring in more reserves as the supply was used.

Mr. Hayes said he agreed entirely. As he had commented on other occasions, he felt that the Committee should not overemphasize net borrowed reserves.

Mr. Johns said he hoped the Committee would not permit proposals such as those advanced by Mr. Balderston and Mr. Bryan to be laughed out of court by attaching a "mechanistic approach" label to them. He felt that any such proposals were worthy of serious study.

Chairman Martin then said that it appeared the majority of the Committee would prefer to retain the directive in its present form. As to the matter of policy under that directive, one possibility would be again to go around the table on the question of "slight but not visible" easing.

After a summary by Mr. Sherman of the positions expressed on the directive by the members of the Committee, the Chairman raised the question whether, in tackling the problem of degree, there was anything further the Committee members could say that would be helpful to the Desk or whether the essence had not already been expressed.

Mr. Leedy said he thought the discussion had told the story quite well.

Mr. Rouse agreed and said that he was satisfied, and no further comments were heard.

Mr. Mills asked that he be recorded as again favoring a change in the directive to substitute the language he had suggested for clause (b) at the past several meetings. This would involve providing for "fostering sustainable economic growth and expanding employment opportunities while guarding against inflationary credit expansion."

Mr. King asked whether the forthcoming period would not provide an excellent opportunity for the Committee, through not mopping up reserves, to evaluate the true state of the situation.

It seemed to him an opportunity to find out, by not creating additional restraint, what the trend of natural forces would be if the System let them develop.

Mr. Robertson commented that the Manager should understand that this was not the will of the Committee.

Mr. Rouse then commented that the Desk might be putting reserves into the market next week. On the basis of the figures alone, one might feel that the Desk should be drawing out reserves. It might be a confusing situation. It would seem necessary to play by ear to a considerable extent.

Thereupon, upon motion duly made and seconded, the Committee voted, with Mr. Mills voting "no," to direct the Federal Reserve Bank of New York until otherwise directed by the Committee:

(1) To make such purchases, sales, or exchanges (including replacement of maturing securities, and allowing maturities to run off without replacement) for the System Open Market Account in the open market or, in the case of maturing securities, by direct exchange with the Treasury, as may be necessary in the light of current and prospective economic conditions and the general credit situation of the country, with a view (a) to relating the supply of funds in the market to the needs of commerce and business, (b) to restraining inflationary credit expansion in order to foster sustainable economic growth and expanding employment opportunities, 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.

In accordance with the understanding at the Committee meeting on January 12, 1960, there had been distributed, with a covering memorandum from Mr. Young dated February 5, 1960, a memorandum of the same date from a staff group consisting of Messrs. Thomas, Rouse, and Young with regard to the continuing operating policies of the Federal Open Market Committee. Attached to the staff memorandum was a suggested revision of the three operating policies. The revision was intended to be generally consistent with the statements of policy in the form reaffirmed by the Committee on March 3, 1959, but endeavored to provide additional flexibility for meeting operating problems in the market. The manner in which the proposed revised language might be applied toward making Open Market Account purchases of the 2-1/2 per cent Treasury bond of 1961 as a means of helping the Treasury minimize its refunding difficulties was outlined in the memorandum.

Chairman Martin commented that no action on the proposed revised operating policies was called for at this meeting but that it seemed appropriate for the members of the staff committee to make any statements they might desire.

Mr. Thomas said that the staff committee did not presume, in the absence of more direction from the Open Market Committee, to make any change in the basic nature of the operating policies. However, it had suggested some changes in wording that might permit a little more flexibility in operations, and in any event should clarify the extent to which there could or could not be flexibility in operations. The proposed revision also endeavored to clarify what to some seemed to be the important point that these operating policies were in a sense working procedures and not inviolate rules. It attempted to make clear that the Open Market Committee at any meeting could give any direction it desired as to what procedures were to be followed without this being interpreted as establishing a new precedent or making a drastic change. In going over the rules, the staff committee tried to clarify to what extent action could be taken on the 2-1/2 per cent bonds of 1961 within the framework of the operating policies and the extent to which action with respect to that issue would require special authorization by the Open Market Committee. In general, the conclusion was that as soon as the bonds had become "short term"--and in this respect the Open Market Committee might want to make a more precise definition--they could be purchased or sold in the same way as any other short-term securities. However, any operations of that sort could not be very large without making quite a substantial change in the Open Market Account portfolio, at least the portfolio of Treasury bills. Therefore, any substantial move to acquire the 2-1/2 per cent bonds would, and probably should, require special consideration by the Committee. The intent of the staff committee was to open up discussion by the Open Market Committee, which might or might not want to recommend a more thorough review of the operating procedures.

Mr. Young said one of the aspects of the matter the staff committee had in mind was the public relations angle, because the current statement of operating policies had been referred to in some quarters as unduly limiting and doctrinaire. The staff had tried to find language which would take away some of that implication while retaining basic principles and at the same time providing flexibility to the degree that experience had suggested some flexibility might be desirable.

Mr. Rouse said he thought it would be necessary to provide a different definition of short-term securities in order to take the suggested action with respect to the 2-1/2 per cent bonds. At present the nearest thing to a definition was in the case of repurchase agreements, where 15 months is prescribed. Almost any definition that the Committee might adopt would have to be arbitrary. The period could be almost anything up to five years. Because banks generally use maturities up to two years to adjust their reserve positions, one possibility would be for the Committee to go up to two years and adjust the rule on repurchase agreements accordingly. If such a definition were made, the Account presumably would deal in all such securities, not only in the 2-1/2 per cent bonds. It would ask for bids or offers on such securities, as the case might be, and not specify one issue such as the 2-1/2 per cent bonds.

Mr. Rouse saw no point in changing the language of the operating policies unless there was a change under which actions could be taken that would relieve the kind of criticism that had been directed at the Committee.

Mr. Young noted that the criticism went to matters of substance as well as semantics.

Mr. Hayes expressed the hope that any change would be more than merely a change of language and would be in the direction of signifying an actual willingness on the part of the Committee to be flexible, as exemplified in certain decisions during the past several months to make exchanges of maturing issues in part into longer issues, and also as exemplified by the Chairman's statement to the Joint Economic Committee last summer.

Mr. Mills said he would offer at this time only the comment that adoption of the suggested wording would represent an abject recantation of error. He placed a more sweeping connotation on the proposal than did Mr. Hayes. Fundamentally, the question was one of deciding whether a "bills only" policy had been completely incorrect and should be jettisoned in favor of a policy that would permit operations in all areas of the Government securities market. He granted that no member of the Committee should want to be doctrinaire, but this proposal contemplated a vast change from the philosophy under which the Committee had been operating for the past several years.

Mr. Allen said he would make no comment on the proposed changes that he thought were improvements. He noted, however, that paragraphs (b) and (c), in their revised form, each concluded with a clause stating that exceptions to the general operating policies stated therein might be made at any time upon express authority of the Federal Open Market Committee. To him, the right to make exceptions was inherent in the powers of the Committee. If the majority felt that for public relations reasons it was important to mention this, he would do so only once, by eliminating the final clause in (b) and (c) and adding that clause as a new paragraph (d).

Mr. Allen then referred to the fact that paragraph (a), as proposed, would state that it was not the policy of the Committee to support any pattern of prices and yields in the Government securities market and that operations in the Government securities market were primarily to effectuate the objectives of monetary and credit policy. (The present language states that intervention in the Government securities market is solely to effectuate the objectives of monetary and credit policy (including the correction of disorderly markets.).) He recalled that the Committee had accepted paragraph (a) in its present form with no dissenting votes, and said that he would prefer to continue to use the word "solely." Similarly, in paragraph (c) he would prefer not to substitute "primarily" for "solely". In the past, he observed, there had been only one dissent from the wording of this policy. As to the portion of the revised paragraph (b) which would state that open market operations were to be conducted in short-term securities (principally but not exclusively Treasury bills), he would prefer to retain the present language which states that 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).

Mr. Johns inquired as to the purpose of changing "solely" to "primarily" in paragraph (a). Since the current statement was adopted, the Committee had been averring that transactions in the open market should be conducted solely for the purpose of effectuating the objectives of monetary and credit policy (including corrections of disorderly markets). As Mr. Allen said, no objection had been indicated to the current language; the vote was unanimous. It would appear that the change of wording must be for the purpose of saying that there was some other reason for conducting transactions in the Government securities market than that of effectuating the objectives of monetary and credit policy, and he would like to know what those other objectives might be.

Mr. Young responded that the memorandum was intended to cover this point. The staff committee was asked to consider the statement of operating policies with a view to the possibility of making some adaptations in operations that might facilitate the refunding problem of the Treasury. The Committee could not very well suggest something that would serve this purpose and leave in the word "solely" so the suggestion was to shift to "primarily." The staff was advancing nothing more than a suggestion; it had simply been reaching for words that might accomplish the aforementioned purpose.

Mr. Thomas noted that the change in paragraph (a) would substitute a general phrase and eliminate reference to a specific practice, namely, the correction of disorderly markets. The language of the present statement is subject to the possible interpretation that the Manager might take action to correct disorderly markets without coming to the Committee, although the minutes of the Committee's meetings clearly require that the Manager must obtain Committee authorization for taking any such action. The proposed revised language is intended to make it clear within the statement itself that the Manager must come to the Committee to obtain authorization for the correction of disorderly markets.

Mr. Bryan said the discussion had made it quite clear that the Committee would gain little or nothing from the suggested revisions unless at the same time it contemplated considerable changes in actual practice. He would not favor adoption of the revised wording until the nature of those changes had been spelled out to him.

Mr. King referred to paragraph (a) of the current and proposed statements and observed that in both versions the statement began by indicating what was not the policy of the Committee. While there might have been reasons for that approach in the past, he wondered whether it was still necessary to start with a negative statement. It seemed to him that it might be preferable to begin by stating what the Committee wanted to encourage.

Chairman Martin then said he hoped the Committee members would try to think the problem through in all of its aspects before the date of the next meeting. He felt that the Committee was quite well united in matters of general operating policy. There were disagreements at times, but the disagreements were not nearly as widespread as they had been at times in the past. The thing for the Committee to do was to think the matter through and to know what it was doing; to think the problem through objectively and to look at it objectively. One reason for instituting the operating policies had been to improve the Government securities market, and the question was whether or not that market had actually been improved over the past several years. That was a logical subject of inquiry. It had been suggested to him by several individuals that the continuing operating policies might be abandoned; that if the Committee met every three weeks perhaps it should not have any continuing operating policies. That was another possible approach. At least the Committee should not put something like this on paper and debate the matter once a year. It was something to be thought through so that the Committee would be clear in what it was doing.

It was agreed that the next meeting of the Federal Open Market Committee would be held on Tuesday, March 1, 1960, at 10:00 a.m.

Thereupon the meeting adjourned.

Ralph A. Young

Secretary

Reserve Target for February

using Total Reserves

(Daily average figures - 000,000 omitted)

(1)	**February growth amount (at 2% annual rate)**		**$ 31** 1/
(2)	**Actual reserves - January**	**$ 18,854** 2/	
(3)	**Deduct normal decline in reserves between January and February**	**(300)**	
		$ 18,554	**$ 18,554**
(4)	**Target for February**		**$ 18,585**
(5)	**February Target range for practical administration of account**		**$ 18,635** **$ 18,535**

1/ February growth amount at 3 percent annually would be 47.0 million; at 4 percent annually would be 62.0 million.

2/ This amount after seasonal adjustment ($18,704) was extraordinarily close to the center of the target range for January ($18,650 to $18,750) suggested at the last FOMC meeting. This circumstance proves nothing; and, indeed, is somewhat regrettable because it prevents at this meeting an experimental attempt to show how short-run overages and underages would be handled in adjusting instructions on a total reserve target basis.

Item No. 1