A meeting of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System in Washington on Tuesday, March 28, 1961, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Hayes, Vice Chairman
Mr. Allen
Mr. Balderston
Mr. Irons
Mr. King
Mr. Mills
Mr. Robertson
Mr. Shepardson
Mr. Swan
Mr. Szymczak
Mr. Wayne

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

Messrs. Bryan and Clay, Presidents of the Federal Reserve Banks of Atlanta and Kansas City, respectively

Mr. Young, Secretary
Mr. Sherman, Assistant Secretary
Mr. Kenyon, Assistant Secretary
Mr. Hackley, General Counsel
Mr. Thomas, Economist
Messrs. Einzig, Garvy, Mitchell, Noyes, Ratchford, and Walker, 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. Knipe, Consultant to the Chairman, Board of Governors
Mr. Petersen, Special Assistant, Office of the Secretary, Board of Governors

Mr. Hilkert, First Vice President, Federal Reserve Bank of Philadelphia

Messrs. Eastburn, Hostetler, Jones, Parsons, and Tow, Vice Presidents of the Federal Reserve Banks of Philadelphia, Cleveland, St. Louis, Minneapolis, and Kansas City, respectively
Mr. Eisenmenger, Acting Director of Research, Federal Reserve Bank of Boston
Mr. Brandt, Assistant Cashier, Federal Reserve Bank of Atlanta
Mr. Stone, Manager, Securities Department, Federal Reserve Bank of New York

The System Account Manager had submitted the following memorandum to the Committee under date of March 21, 1961, recommending participation by the Account in the Treasury's then impending advance refunding offering:

> The System Account holds the following amounts of the issues eligible for exchange into the new 3-3/8's of 1966 and 3-5/8's of 1967 in the current Treasury advance refunding:

	Amounts in thousands
2-1/4% Treasury bonds maturing June 15, 1959-62	$ 319,849
2-1/4% Treasury bonds maturing Dec. 15, 1959-62	693,765
2-5/8% Treasury notes maturing Feb. 15, 1963	34,000
2-1/2% Treasury bonds maturing Aug. 15, 1963	11,500
Total	$1,059,114

> Among the advantages of exchanging some portion of these holdings is that it would be regarded by the market, the Congress, and the Treasury as helpful to the Treasury in achieving a better balanced debt structure and would reduce the Treasury's burden of refunding the outstanding issues at maturity. From the System's standpoint, there appears to be some advantage in acquiring some holdings of each of the short and intermediate issues to achieve a balanced portfolio. At present the Account holds only $170 million of fixed maturity issues maturing in 1965 or beyond.

> Among the disadvantages is that an exchange would involve some reduction in liquidity of the System Open Market Account, but this is not a serious drawback since the Account will still have very large short-term holdings, $17.9 billion excluding Treasury bills, maturing before the end of 1962. The System should not acquire too large a portion of the new issue through exchange but should limit the exchange to a moderate amount.

> Since there appears to be some advantage and no material disadvantage in exchanging some part of the System's holdings of the issues in question, a partial exchange appears appropriate. The holdings of 2-5/8% notes of 1963 and 2-1/2% bonds of 1963 are too small to be significant in the exchange and might be of some future use in their present form. The System's holdings of the 2-1/4's of June 1959-62 are only 6% of that issue but the holdings of the December 2-1/4's are 20% of that issue. Exchange of about one-half of the December issue would leave the holdings of June and December issues about equal. The Manager of the Account, therefore, recommends the exchange of $350 million of the December 2-1/4's of 1959-62 into 3-5/8's of November 1967. This amount represents about 33% of the $1,059 million total System holdings eligible for the exchange.

This memorandum was supplied to members of the Committee then located in Washington, to Mr. Trieber, alternate for Mr. Hayes, and by telegram to Messrs. Allen, Irons, Swan, and Wayne, respectively, asking for their comment on and their approval or disapproval of the Manager's recommendation.

> The recommendation of the Manager of the System Account that $350 million of System Account holdings of 2-1/4 per cent Treasury bonds maturing December 15, 1959-62, be exchanged into 3-5/8 per cent bonds to mature November 15, 1967, as offered in the Treasury refunding, was approved. Votes for this action: Messrs. Martin, Allen, Balderston, King, Mills, Robertson, Shepardson, Swan, Wayne, and Treiber, alternate for Mr. Hayes. Vote against this action: Mr. Irons.

In voting against the System Account Manager's recommendation, Mr. Irons expressed the belief in a telegram to the Secretary of the Committee that an informed market and the Treasury would recognize that there would be no appreciable improvement in the balance of the debt structure nor a lessening of the refunding burden as a result of a System exchange of a portion of its holdings. Also, in his opinion, the residual holders of exchangeable securities after the completion of the advance refunding would be largely seekers of liquidity, and, consequently, the ultimate refunding for such holders at maturity might be expected to include relatively short-term securities into which the System would roll over without consequence or without creating a problem for the Treasury, especially in view of the relatively small System holdings of exchangeable issues.

Mr. Irons' telegram also expressed the judgment that it was not important that the System build up its holdings of intermediate-term securities. Actually, there was a more significant need to build up holdings of very short-term securities, those in the 90-day to 6-month area, since, except in the case of future swaps, which should be negligible, the System had no probable need for intermediate-term securities. Also, he believed that a central bank's portfolio should be in very liquid securities and no deliberate attempt should be made to lengthen the maturity composition without good and compelling reasons.

Mr. Irons felt that System participation in the advance refunding would imply positive and continuing acceptance by it of the recent experimental policy of dealing in other than short-term securities, and this was beyond the position he would want to confirm at this stage. To the extent that the System must acquire intermediate-term securities, he would prefer that it be done through market purchases at an appropriate time, seeking particular rate effects, rather than through an exchange under advance refunding where there was no significant advantage to be gained.

Mr. Irons considered it unimportant that the System hold significant amounts of intermediate-term securities because it was unlikely (except to the extent of occasional swaps) the System would be a seller of these issues and, in effect, put downward pressure on prices of Government securities. It would seem more likely System operations would be on the buying side, as they had been in the current experiment in the intermediate- and longer-term areas.

> Upon motion duly made and seconded, the action of the members of the Federal Open Market Committee on March 22, 1961, in approving, with Mr. Irons dissenting, the recommendation of the Manager of the System Account that $350 million of System Account holdings of 2-1/4 per cent Treasury bonds maturing December 15, 1959-62, be exchanged into 3-5/8 per cent bonds to mature November 15, 1967, as offered in current Treasury refunding, was ratified, approved, and confirmed.

Before this meeting there had been distributed to the members of the Committee a report of open market operations covering the period March 7 through March 22, 1961, and a supplemental report covering the period March 23 through March 27, 1961. Copies of both reports have been placed in the files of the Committee.

Supplementing the written reports, Mr. Rouse commented as follows:

> With the money market generally easy during most of the period since the last meeting of the Committee, little in the way of open market operations has been required to maintain

an even keel, and the System has been able to stay out of the market while the Treasury's advance refunding was under way. Early in the period, a moderate volume of reserves was supplied through outright purchases of Government securities and through repurchase agreements. Later on, some massive shifts of balances among foreign central banks resulted in substantial net acquisitions of Government securities by foreign accounts, part of which were supplied by sales from System Account in order to mitigate the impact on already declining Treasury bill rates. The large activity in foreign central bank balances, reflecting movements of funds through the foreign exchange markets following the revaluation of the Deutsche mark and the Dutch guilder, proved more troublesome to the Management of the Account than has been the case in some time, and it appears possible that the activity in these accounts will continue to complicate our operations.

Short-term interest rates moved lower through much of the period, with the three-month bill rate at 2-1/4 per cent bid last Wednesday, compared with 2.45 per cent at the time the Committee last met. Money market pressures were remarkably light over the March 15 tax period, while demand for Treasury bills arose from the redemption of tax anticipation bills on March 22 as well as from market switching into shorter-term issues and the foreign account activity mentioned above. Bill rates rose somewhat over the past two days, after the Treasury announcement that it would raise $1.5 billion in cash through an auction of September tax anticipation bills that will take place this afternoon, and an additional $300 million through additions to the regular weekly auctions. Long-term rates moved down somewhat earlier in the period--partly in response to System operations--but the Treasury's advance refunding reversed these price movements, with the net result that long-term rates are not far different now from the levels prevailing before the System's special operations were undertaken. It was of course obvious that the advance refunding would have this impact on intermediate- and long-term rates, but the Treasury felt, and rightly so, that this was a reasonable price to pay to achieve a better distribution of the public debt, particularly from the standpoint of convincing foreigners that the Government meant what it said about putting our fiscal affairs in order. The $6.2 billion in debt extension that the Treasury was able to effect generally exceeded what the market had expected. The success of the advance refunding, in market conditions that were somewhat less than perfect, has solidly established this technique as the Treasury's main weapon in bringing about a better debt distribution.

As to our own operations in longer-term securities, the market generally has come to take a more balanced view of our activity, although the extensive public discussion of our objectives--and the various interpretations placed upon these objectives--has continued to hamper our operations. The market has not yet become fully accustomed to normal System activity in the intermediate area. Last Thursday, for example, we found that our attempts to acquire a moderate amount of such securities on a go-around basis met with only $54 million of offerings, and led to a significant withdrawal of offers and bids that were in the market prior to our operations, as potential buyers and sellers moved to the sidelines to see what the result of our activity would be. We have found that the go-around, and the publicity that goes with it, tends to change a negotiated market into an auction market where the appearance of a potentially large buyer tends to dry up other bids and offerings. As a result, the go-around has not been generally successful, as the reports of these special operations, which have been circulated to you, have pointed out. A major difficulty is that it is well-nigh impossible to prevent word of our go-arounds from spreading widely and rapidly throughout the investment community. The consequence is that potential sellers tend to withdraw from the market in hopes of getting higher prices and potential buyers to withdraw because they are reluctant to follow any upward price movement that might develop in the wake of our operation. The second major difficulty is that dealers normally carry only modest positions in the area in which we are now working, and in the time interval within which go-arounds must be conducted, they rarely could develop the offers or bids that are desired even if there were no knowledge of our activity available to the investing public. Confronted with these difficulties, we have from time to time acquired intermediate securities on voluntary offerings to the Desk, or by purchasing from a limited number of dealers at any one time. In general, these methods have proved more effective and far less disturbing to the market.

Now that the Treasury advance refunding is out of the way, it should be feasible from a market standpoint for the System to continue to acquire longer-term securities in order to supply reserves as they are called for, or to acquire them against offsetting sales of short-term securities to the extent that rate considerations make such transactions desirable. Growing expectations of an upturn in business conditions appear to be resulting in an increasing reluctance of long-term investors to extend their commitments, and this may facilitate purchases for our account and for Treasury accounts.

Returning to the international situation for a moment, our bill rate, even at 2-1/4 per cent, has been competitive with the British bill rate on a covered basis. While the relationship between British and U. S. short-term rates is not an immediate problem, the dollar nevertheless is under considerable pressure in the foreign exchanges, and we cannot afford to relax for a moment, for the present situation could change overnight.

On request by Chairman Martin for any questions concerning the System Account Manager's report, Mr. Robertson said he felt this to be an excellent presentation which he hoped would be recorded in full in the minutes of this meeting. The report brought out the difficulties involved in the System's functioning in the longer-term Government securities market, and he wished to study it further.

Thereupon, upon motion duly made and seconded, the open market transactions during the period March 7 through March 27, 1961, were approved, ratified, and confirmed.

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

In introducing our round-up on the economic situation to the Board yesterday, Mr. Williams pointed out that while considerable factual information on economic developments in February had become available since the meeting three weeks ago, these facts generally confirm the early estimates presented at that time. Hence, most of what the staff reported then, and what I shall say today, will have a familiar ring. It is too soon to say much about March, except that changes in either direction from February are likely to be moderate. We are still estimating that GNP will be around $500 billion for the first quarter.

To cite a few specific developments on which data have become available in recent weeks: industrial production leveled out at 102 per cent of the 1957 average in February; housing starts were up to a seasonally adjusted annual rate of a little over 1,150,000--a considerable improvement from the December low; February auto sales continued at the depressed January rate, but March will almost certainly show some pick-up; with auto production held to very low levels through March, there should be a contra-seasonal reduction in inventories, which will bring dealer stocks well below year-ago levels; used car prices turned up last month after an extended decline; retail sales were up 1 per cent; consumer credit outstanding declined further--probably by a little more than in January; and new orders for durable goods increased 2 per cent. The composite index of leading indicators moved up again.

As reported at the last meeting, the seasonally adjusted unemployment rate was up slightly in February, as the actual number unemployed hit a postwar peak of 5.7 million. Seasonal factors should reduce the actual number unemployed for some months now. For example, a normal seasonal movement would cause a decline of about 300,000 from February to March. Thus, if unemployment in fact declines by less than that amount, as may well be the case, we will see some further rise in the seasonally adjusted rate in March.

The extension of unemployment benefits to longer-term unemployed workers, which was authorized last week, will both relieve the severe hardship suffered by workers in this category and add about $400,000,000 to consumer income in the second quarter.

Without minimizing in any way the unemployment problem, it is important to keep the data in perspective. Therefore, it should be pointed out that employment is as high as--in fact, slightly higher than--it was a year ago. In other words, the increase of 1.8 million in the number unemployed is less than the 2 million added to the labor force in the same period. This contrasts to the substantial decline in employment which occurred from mid-1957 to mid-1958.

Taking all of the new information that has become available since the last meeting into account, there seems to be no reason to modify the earlier observation that we shall see some improvement in the economic situation in the second quarter. If any modification is called for, it is with respect to our assessment of the possible vigor of the upward movement. More and more careful and generally conservative analysts in business and in Government are quietly edging up their estimates of GNP and industrial production for the last two quarters, as the year progresses. To the extent that these forecasts have some influence on businessmen's decisions on inventory policy and other expenditures, they may be self-supporting. Any appraisal of the prospects must take into account the impact of this spreading optimism regarding the outlook, as well as the changes in output and employment which have actually occurred. Nevertheless, it still seems most unlikely that activity will approach critical levels, in terms of sustainability, in the foreseeable future.

It is interesting, in this connection, that one recent survey showed that businessmen's expectations with respect to the likelihood of increases in the price of their own products were near the lowest point for the postwar period. Wholesale prices have remained fairly steady, despite growing optimism as to the outlook, and sensitive materials prices, while they have shown some improvement, are still below the 1953-54 average. The consumer price index has been moving in a very narrow range, reflecting largely seasonal influences--down one-tenth of 1 per cent in January; up the same amount in February; and expected by BLS officials to be down again in March. So far there seems to be no evidence of either inflationary pressures in fact or a strong expectation of inflation in the near-term future.

Mr. Thomas presented the following statement on the credit situation:

Since much of the discussion of Federal Reserve policies recently has been focused on interest rate effects, developments with respect to rates are of particular interest. Contrary to trends in February when short-term rates rose and long-term rates declined, in accordance with views as to System objectives, opposite trends have been observed in March. For an explanation of this perversity, it is necessary to look to market developments and expectations, rather than Federal Reserve operations. Whether the System should or could have brought about different results is at least questionable.

Factors causing the declining tendency in short-term rates include the somewhat smaller volume of business cash needs than is customary during March; the redemption of outstanding tax bills, which reduced the available supply of short bills and created a reinvestment demand; some exceptional demands for bills from foreign accounts; actual and prospective acquisition of short-term securities by the American Telephone and Telegraph Company; lessened selling pressure by dealers following sharp reductions in their portfolios during late February and early March; and the pressures and the uncertainties in the longer-term markets which induced investors to prefer short-term securities. Finally, reserves were available in moderate amounts and the money market was easy during the period when it is ordinarily tight.

Increases in medium- and long-term rates reflected principally the growing view that economic activity may turn up soon, bringing increased credit demands; the congested state of the municipal bond market, where dealers held large inventories of unsold issues with more in prospect; and the anticipatory effect of large Treasury borrowing demands during the remainder of the year. The American Telephone and Telegraph offering of new stock to its shareholders may have directly or indirectly been absorbing some funds that might have been invested in other long-term securities. The Treasury advance refunding operation confirmed views that some of the Treasury borrowing would be done in the longer-term sectors either directly or through such an advance operation. While the bulk of the exchanges of $6 billion are believed to represent holdings that would not otherwise have been disturbed, some of them might have some future effect on long-term markets.

Bank credit demands during the first three weeks of March, using partial figures for the past week, appear to have been somewhat smaller than usual in that period. Total loans and investments at city banks declined on balance. Business loans increased about as much as usual, but loans to finance companies showed a contra-seasonal decline. Reflecting a reduction in dealers' inventories, loans to dealers in Government securities also declined by a sizable amount, as did city bank holdings of Treasury bills and also of Government securities maturing after one year. Holdings of other securities increased.

Money supply, seasonally adjusted, which increased sharply in January, has shown little further growth since the beginning of February. The average for the first half of March was only slightly larger than a year ago. The situation in the third week of March is uncertain owing to lack of complete data and the difficulty of appraising the effects of the timing of tax payments. Figures for the single date of March 15 and partial data for city banks for March 22 (just before the tax payments are drawn and certainly before they are paid) indicate that private demand deposits were relatively large on those dates. Time deposits at commercial banks continued to increase during February and the first half of March and are more than 10 per cent larger than a year ago. Shares in savings and loan associations have increased in the past year by nearly 15 per cent, with the expansion continuing during the first two months of this year.

Reserves have been available to member banks during the past month in amounts adequate to support seasonal changes in deposits, but not enough to provide for further growth unless banks reduced their excess reserves. Free reserves, in fact, have declined somewhat since the latter part of February and have been much less than in December and January. It is estimated that during the latest week--that ending March 22--a sizable portion of the available reserves were being held against temporarily large United States Government deposits. As these deposits are drawn down, as they are scheduled to be in the course of the next four weeks, funds become available for bank credit reduction or private deposit expansion. An over-all contraction is to be expected this week and next, but the required reserves released will be absorbed by a decline in float and by Easter currency demands.

Unless some additional reserves are supplied to allow for monetary expansion or unless a gold outflow is resumed (neither of which is assumed in the projections presented), no sustained additions to Federal Reserve credit will be needed until July. On the basis of recent experience, however, it is questionable whether free reserves of $500 million or less provide an adequate stimulus to bank credit expansion. Therefore, to foster monetary growth, System operations in the course of the next two weeks may require net purchases of nearly $300 million of securities, which may be followed by sales of around $500 million in the third week of April, and then fluctuate back and forth from then on through June.

From a longer-run standpoint, the Committee will need to give some thought to the course of policy in case the expected economic recovery is actually beginning. In view of many long-run and structural weaknesses in the economy, the recovery may not be particularly robust or threatening of speculative excesses. It is more likely to require recuperative therapy, rather than restraint. The fostering of some bank credit expansion and greater than seasonal monetary growth will no doubt be appropriate for the remainder of this year.

With respect to interest rates, there is a popular view that any economic recovery will bring about a rise in both long-term and short-term rates. This view is based in part on expectations as to credit demands and in part on beliefs as to shifts in monetary policies. This may not be a necessary conclusion. Although pressure for further declines in short-term rates might come to an end, it is not certain that a marked rise in interest rates will accompany the earlier stages of recovery.

In the first place, interest rates are now much higher than they have been in any other postwar recession period and are not unlike those of the recession periods in the 1920's. Hence a sharp reversal such as occurred in 1958 seems unlikely. Secondly, various estimates or projections made by the Board's staff and by others indicate that, with a moderate pace of economic recovery--which may be all that should be expected--over-all credit demands are not likely to be particularly heavy this year. The total of private demands is indicated to be less than in any other year since 1957 or perhaps earlier, and when Federal Government borrowing is included, the total is about the same as in 1960--much less than the high level of 1959 and also well below 1958 and 1955. Demands are expected to be quite light in the short-term credit area and moderate in the long-term sector.

Financial savings available for investment, moreover, have expanded in recent years and are expected to continue in large volume during 1961. Most of these funds are available for long-term investment. Estimates of the cash flows and liquidity needs of nonfinancial corporations indicate that not only will their credit demands be moderate, but also that they will probably have funds for the purchase of securities. It appears that funds from these and other sources will be adequate to meet credit demands without requiring direct investment by individuals of the magnitudes of recent years. Consumers may want to add to their holdings of cash, as well as to those of other fixed value redeemable claims such as savings deposits and shares.

These various factors point to the absence of strong pressures toward rising interest rates during the months ahead, unless economic recovery exceeds expectations and strong speculative tendencies develop. Major influences that might determine the course of interest rates will be the borrowing demands and debt-management policies of the Federal Government and the availability of bank credit.

The latest budget estimates just presented by the Administration, though differing in many details, seem to confirm, rather than alter, the estimates of the Board's staff as to the Government's financing needs for this calendar year, when allowance is made for portions in the Administration's estimates as yet incomplete or uncertain.

Net cash borrowing for this calendar year is now projected at less than $5 billion (around $4.5 billion), but the total of all new borrowing, not including that to refund maturing issues other than tax bills, may exceed $15 billion. Of this total, some $2.7 billion has been completed or already announced. If the May refunding is so handled as to avoid attrition, further borrowing might be unnecessary until July. In the last half of this year, net borrowing will approach $10 billion and gross borrowing may exceed $12.5 billion. These needs are comparable with those of similar periods in 1958 and 1959, although the calendar and fiscal year total will be less than in those years. Also, as previously explained, total public and private credit demands in the last half of this year are not expected to be as great as in the corresponding periods of 1958 and 1959.

The effect of Treasury borrowings on the structure of interest rates will depend to some extent upon the maturity distribution of the securities offered to raise new cash and to refund maturing issues. Some debt extension would be desirable to mitigate financing problems in the next few years. In view of the prospects for savings and for moderate private demands for long-term credit, limited extension of the Federal debt might be possible without undue upward pressure on long-term rates. Corporate funds should be available to absorb some of the short-term borrowing. The bulk of the Treasury borrowing, however, could appropriately come from the banking system.

Even though savings are expected to be rather large and credit demands only moderately large, all these demands cannot be met without fairly sizable expansion of bank credit. In the absence of bank credit growth, interest rates would have to rise sufficiently to bring forth more saving or additional nonbank investment in Government securities. Any such rates might unduly retard the developing recovery. In view of the moderate growth in the money supply during the past two years, an increase of at least 3 per cent, or $4 billion, would seem to be essential this year. Time deposits at commercial banks might be expected to increase by as much as $5 billion.

The total of commercial bank and Federal Reserve credit expansion in 1961 may well exceed $10 billion--concentrated in the last half of the year. Bank loan demands are expected to be moderate throughout this year. The banking system should be in a position, therefore, to supply a substantial portion of the Federal Government's borrowing needs during the remainder of this year, without undue credit expansion or monetary creation. Perhaps as much as $8 billion of the $10 billion net expansion in Government debt in the last half of the year might be supplied through commercial bank and Federal Reserve credit. Some $2 billion of Federal Reserve credit will be needed during the remainder of the year to cover seasonal monetary and currency demands and to allow for some growth. At least half of this increase will not be needed until the last few weeks of the year, but additions averaging around $100 million a month would be appropriate between now and November.

It should be possible to provide reserves for such an increase in bank credit without keeping interest rates at too low a level, given moderate economic recovery. In fact, that amount of bank credit may be necessary in order to avoid too sharp a rise in interest rates that would retard the recovery. Reserves may be supplied through purchases of short-, medium-, or long-term securities, depending upon the nature of market pressures at the time of the transactions and with due regard to proper administration of the Account.

In reply to a question from Mr. Allen concerning the extent to which the Treasury might be in the market between now and the May refunding, Mr. Thomas said that the Treasury would not be in the market except for the refunding of the April 15 bill and the auction of tax anticipation bills that was to be held today. There was also the small increase in the amount of weekly bill offerings that recently had been announced.

Mr. Hayes presented the following statement of his views on the business outlook, credit policy, and related matters:

For a good many months now the Committee has been forced to keep a careful eye on both the need for resisting domestic recessionary tendencies and the need to avoid aggravating a sharply adverse balance-of-payments situation by allowing short-term interest rates to fall to excessively low levels. On the whole, I feel that we have been rather successful in coping with this dual problem. But on neither front has the battle yet been won, and I think it would be a dangerous error to assume that it has. I was somewhat concerned at the last meeting by the impression I gained that some members were inclined to let up on the objective of keeping short-term rates up--say around the 2-1/2 per cent level--presumably on the ground that the difficulties of the dollar are largely behind us. I shall try to demonstrate a little later why I do not share such a view.

Of our two major problems, I am inclined to the opinion that the domestic recession may prove to be the more tractable. While the prevailing tone of growing business optimism may be somewhat premature, there have been further indications in the last three weeks that we are at or close to a bottoming out of the recession. A number of key series that had been falling for some time have either leveled out or turned upward. I am thinking of such items as new orders for durable goods, manufacturers' sales of durables, industrial production, and retail sales--and the smallness of the expected decline in business plant and equipment spending is also encouraging. On the other hand there has been no significant change in the housing or inventory situation, and in general there are as yet no signs of emerging strong private demands. Furthermore, unemployment seems likely to stay disturbingly high even through many months of recovery.

In the field of bank credit, the February statistics for all commercial banks generally confirm earlier indications of considerable gains in total bank credit, total loans, and business loans--and early March data point in the same direction, with tax borrowing rather heavier than had been expected. Figures on the public's liquidity and on bank liquidity suggest that our policy of credit ease is continuing to produce desired results. On the other hand, the slower recovery of bank liquidity in this than in previous recessions will make it less necessary for the System to absorb excess liquidity during the coming expansion.

As far as the domestic economy is concerned, it seems to me clear that, at least until the probable configuration of the recovery shapes up fairly clearly, we should maintain credit ease and should continue our attempts to nudge long-term rates lower or, at the very least, to exercise some "braking" influence on any rise in such rates if expectations of business recovery induce considerable selling of longer-term securities. (Fortunately the volume of weak holdings of longer-term securities overhanging the market appears to be much less than in 1958.) At the same time there is nothing in the domestic picture to suggest a need for lower short-term rates. Downward pressure on such rates may develop in any case if sellers of long-term securities temporarily invest at the short end to wait out the transition to a new equilibrium; but there is no reason why we should try to push down the short rate, and no harm should result to the domestic economy if, because of international considerations, we try to hold short rates where they are or even try to press them higher.

Turning to the international situation, I would like to point out a number of reasons why we cannot afford to be complacent:

(1) Although the over-all balance of payments improved sharply in January, with indications of a \$100 million surplus for that month, this was followed by an indicated deficit of some \$200 million in February, and there is some evidence that this adverse trend has continued in March as a result of the backwash from the mark revaluation. On balance, the first quarter figure will show an appreciable improvement over the last two quarters of 1960, but not nearly enough to quiet foreign anxieties.

(2) The recent minor increases in the gold stock reflect special circumstances rather than any strong underlying trend toward restoration of confidence in the dollar.

(3) Confidence in the stability of exchange parities in general has been sadly disrupted by the recent mark and guilder revaluations. Net transfers of funds across the European exchanges during the first week after these events probably approached \$1 billion. The exchange markets remain in a state of acute anxiety, with rumors continually circulating of further exchange rate moves to be expected. For example, there is a widespread belief that if a renewed heavy flow of funds to Switzerland should occur--and any number of political or economic events could touch it off--the Swiss might be forced into a revaluation, perhaps followed by other currencies. The dollar has been conspicuously weak on the European exchanges, especially in Frankfurt. Fortunately the speculative capital movements have so far been largely confined to transfers by foreigners. But a much more serious situation, comparable with that of last fall, could develop if United States residents should jump into the game.

(4) To some extent we have been benefiting from the weakness of the British position rather than from a basic improvement in our own. While we have seen some return flow of foreign funds to the New York stock market, there have been no significant indications of renewed foreign interest in either short- or long-term U. S. Government obligations.

(5) The delicate political and military international situation makes it all the more important that we do all we can to strengthen the position of the dollar.

The level of our bill rate has a very important effect on foreign market psychology, quite aside from the arithmetic relationship of our rate to market rates abroad. I believe that the rate of 2-1/2 per cent reached a few weeks ago conveyed an encouraging impression of our determination to halt further outflows. In the judgment of some foreign central banks, a bill rate in the 2-3/4-3 per cent range would be of very real psychological value.

All of this suggests to me that we would be fully justified in giving primary consideration to the bill rate over the next three weeks, of course within the same general framework of credit ease in which we have been operating. I think it would be highly desirable to see the rate rise appreciably above the present level. If, as seems likely, open market purchases are required to maintain free reserves somewhere around the $400-$500 million level in the next week or two, I would hope that the Manager would be able to use longer-term securities for the bulk of this operation, having in mind also the added advantage of exercising some influence on longer-term rates. And incidentally, it seems to me that we have now been operating outside of the short-term area for a sufficient period so that we might now appropriately authorize the Manager to use his discretion in choice of maturities, without being confined necessarily to a maximum maturity of 10 years.

I can see no reason to consider a change either in the discount rate or in the directive.

Mr. Ellis said that although some First District figures showed continued weakness, spending seemed to be holding up, or even gaining. Even after adjusting for Easter dates, department store sales looked good, and it appeared that Easter sales might come close to last year's record high. Automobile dealers had experienced a pickup in sales, and a recent survey of capital expenditure plans indicated that there was a good chance that expenditures for the current year might equal 1960. The strength in these expenditure figures was traceable to electronics and aircraft. Bank debits were up 3 per cent from a year ago. Average weekly hours in manufacturing were above the national average in all District States and were up since the first of the year, while average weekly earnings were up from January to February. On the other hand, the drop in employment in February, while a little less than last year, was still significant, and unemployment was continuing to rise. Although there were no New England cities classified as having more than 12 per cent unemployment, unemployment was some 50 per cent above a year ago. There was no evidence of expansion of output even though corporate loan demand was high. Business loans rose sharply over the March tax date, and for the year to date the increase matched the 1960 gain, which was a record for the District. Deposits had risen a little more slowly, so the average loan-deposit ratio stood .4 per cent above the year-ago level. Thus, in that sense liquidity had not been restored. District banks were net buyers of Federal funds during the past few weeks, reflecting particularly the seasonal situation as to demand deposits, but borrowing from the Reserve Bank was at a low level. Two Boston savings banks reported a lowering of the average mortgage rate in February, but one bank outside the city raised its average rate by 1/4 per cent.

As to policy, Mr. Ellis said he viewed credit conditions in the past three weeks with considerable satisfaction. Free reserves had been above $500 million on average, and the bill rate had averaged closer to 2-1/4 than 2-1/2 per cent, which was in sympathy with the position he had expressed three weeks ago. The covered spread between the U. S. bill rate and the British bill rate had been narrowed to such an extent that the incentive to move short-term capital was substantially reduced. Therefore, although the Boston Bank was not as close to the foreign credit situation as the New York Bank, in the absence of a gold outflow he would lean in the direction of feeling that a bill rate of around 2-1/4 per cent would be preferable to a level of 2-1/2 per cent. Perhaps the hazard of a further gold outflow was small enough to permit providing a little more ease and increasing the level of free reserves, thus continuing some of the thrust of monetary policy toward stimulating credit expansion domestically. As stated in the report of Mr. Noyes, there seemed to be no evidence or expectation of inflationary pressure and no sharp credit expansion seemed imminent. From that standpoint, therefore, the hazards of providing more reserves did not seem to be too great.

In his opinion, Mr. Ellis said, any change in the discount rate at this time would be ill-advised. As to the directive, his reading of the comments submitted to the Ad Hoc Subcommittee seemed to indicate a rather general approach toward separating the directive into two parts, and rather general agreement on rephrasing one part of the directive more frequently to reflect changes in economic conditions that should be met by appropriate changes in open market policy. He had a feeling that the general thinking had been to postpone changing the current directive looking toward the time when a fundamental change in the form of the directive might be made. However, if the Committee did not get to a decision on major issues, he would suggest that some consideration be given to a change in the current directive so that it would provide for fostering recovery rather than sustainable growth.

Mr. Irons reported a generally satisfactory level of economic activity in the Eleventh District, with activity in some areas increasing. Department store trade was good and construction was up from the preceding two or three months. There was a lot of substantial construction going on in some parts of the District, the situation in Houston being particularly outstanding. In view of the more open weather ahead, the prospect was for further improvement. Agricultural conditions appeared promising, with good agricultural weather prevailing. There had been some further increase in unemployment, although employment was running above a year ago. Crude oil production was up in the past month, but probably would be off this month, production having been dropped back to a nine-day allowable basis. Stocks could get out of hand quickly, and there would be further cutbacks if that were to happen.

As to banking, loans and demand deposits were up while investments were down during the past three weeks. The banks were not highly liquid, but they were in a reasonably liquid position. District banks were net sellers of Federal funds during the past three-week period, and there had been virtually no borrowing at the Reserve Bank for most of the period.

On the whole, Mr. Irons said, the District situation was not too different from the situation that appeared to be developing nationally. As to attitudes, he believed a general feeling had developed that 1960 was not too bad a year--better than people had thought. There seemed to be a cautious optimism with regard to 1961.

Mr. Irons expressed the view that during the past three weeks the Desk had done a good job in trying to accomplish the twin objectives of policy, that is, to keep reserves adequately available and to avoid too much downward movement in the short-term rate structure. Although he had advocated a short-term rate of around 2-3/8 or 2-1/2 per cent, he was not too sorry to see the bill rate move down a bit, for this would indicate that the System had not been deliberately trying to peg the rate. As long as the rate was within a range consistent with the international picture and the economic situation, he would favor letting it move with the market to some extent.

In summary, Mr. Irons said, he viewed the situation with reasonable satisfaction. He would like to see a continuation of about the same degree of availability of reserves, recognizing at the same time that the short-term rate was an important factor and should be watched closely. As to the level of free reserves, he would think in terms of $400-$500 million rather than $600-$700 million, but he would not be too concerned about the precise figure because he did not consider it too meaningful. He would not favor any change in the discount rate, and he did not feel too strongly about a minor change in the directive. On balance, however, he would prefer to leave it alone.

Mr. Swan stated that Twelfth District economic behavior, over all, was much the same as nationally. There were some additional indications of improvement, not so much actual as potential, in various areas, but these were coupled with continuation of a far from satisfactory unemployment picture. Although February saw the first gain in aircraft employment since January 1959, this was a small gain and was related to a particular concern. Generally speaking, the unemployment picture was a little less satisfactory in February than in January. On the other hand, steel production had continued to pick up; the increase in February, and apparently in the first part of March, was considerably greater than for the country as a whole. Perhaps the major source of optimism in the past three weeks was the strengthening that occurred in lumber and plywood. There had been a considerable increase in new orders, although from a very low level, and the increase was followed rather quickly by a firming of prices, also from a low level. It was not known exactly what this upturn in orders reflected, other than some restocking of low inventories by distributors and industrial users; the basis for a sustained increase in demand was not in the picture as yet. Nonresidential construction had been well sustained, but there were few indications of changes in builders' plans that would portend a sustained increase in home building in the months immediately ahead, this despite some further indications of increasing availability and lower cost of mortgage funds. Mortgage brokers reported a considerable increase not only in the availability of funds but in the interest displayed by Eastern investor in Western mortgages.

Mr. Swan said that major District banks had been in a fairly easy position during the last few weeks. They were net sellers of Federal funds by a small margin during the past week, and there was an indication that sales would be considerably larger relative to purchases in the current week. Borrowing from the Reserve Bank was minimal. Savings deposits continued to rise rather steadily, and somewhat more substantially than would have been guessed several months ago. The favorable experience of the two smaller banks that pioneered in the crediting of interest on a daily basis, along with the spread of this practice to some country banks, had now led all major banks on the West Coast to announce that they would be on a daily interest basis as of the first of April.

Mr. Swan said that he would not argue for any overt change in policy at this time. He thought that developments had reflected about what was indicated at the meeting three weeks ago. However, he was substantially in agreement with Mr. Ellis in hoping that, if anything, conditions might be just a little easier and that additional reserves would be supplied to the extent possible without putting too much pressure on the bill rate. He would not be concerned if free reserves got back toward, or to, the $600 million level, or if the bill rate reverted to around 2-1/4 per cent. It seemed to him that in view of the auction yesterday and the indication of further

Treasury borrowing in the short-term area, the System might be in a position to increase the availability of reserves somewhat without so much downward pressure being exerted as to push the bill rate below about 2-1/4 per cent in the period ahead. He would not favor a change in the discount rate at this time. Although he did not feel too strongly about the directive, he would have been happier if it had been amended earlier to provide for fostering recovery rather than sustainable growth. Soon, he suggested, it might be too late to make such a change. Therefore, while he did not feel strongly on the matter, on balance he would favor making that change.

Mr. Deming commented that between May 1960 and February 1961 nonagricultural employment in the Ninth District, seasonally adjusted, declined less than in the nation, an occurrence similar to that during the period from August 1957 to April 1958. In large part this more favorable trend was due to the greater stability of District manufacturing employment than in the nation as a whole. The other side of the coin, however, showed that employment expansion in recovery was slower in the District than in the nation, and this same pattern was expected to hold this time. The Minnesota employment people did not expect the State's nonagricultural employment to top year-earlier levels until very late this fall, and not until the spring of 1962 was more than a seasonal gain expected. A significant part of the current unemployment was structural in character and reflected depressed activity in the Iron Range and in the copper country of Montana and upper

Michigan. Not only mining employment, but employment in closely associated lines, particularly transportation, was affected.

The Minnesota Poll, to which he had referred on other occasions, had just published its findings on consumer buying plans from a survey taken between mid-January and early February. In general, the findings agreed more closely with the findings of the FRB-Census January survey than with those of the Survey Research Center. Plans for new car buying indicated a sales volume equal to 1959 but down from 1960, while used car buying apparently would be weaker than in either of the two previous years. In contrast, purchases of new houses should equal 1960 but be off somewhat from 1959. More than half of the consumers questioned indicated they would be buying one or more of 18 household appliance or furniture items. Unfortunately, there were no comparable data for previous years.

The snows in the District came late this year and had depressed retail sales in recent weeks. Buying had picked up, however, and in the most recent week for which data were available (the week ended March 18) District department store sales were up, relative to a year ago, more strongly than national sales.

Agriculture continued to be favorable. Cash receipts from sales in January were 18 per cent ahead of last January, in contrast to a 14 per cent gain nationally. As against the five-year average, however, the District's 13 per cent increase in January fell short of the nation's 16 per cent gain. Planting intentions in the District were not significantly different, relative to last year, than in the nation. There had been some moisture recently, which helped the outlook.

In banking, an earlier than usual levelling off of the seasonal deposit outflow at both city and country banks appeared likely. The loan picture was about the same as it was last year, and some bankers expressed surprise that loan demand had been or was becoming so strong. Bank liquidity had improved, but it was still far from previous recession troughs. One interesting, and perhaps frightening, development in recent years was the failure of agricultural loans outstanding to decline in the fall and winter. Thus, the spring build-up started from the high plateau of the previous fall. This probably reflected the pressure of rising costs on declining income, and it might pose problems for farm area bank liquidity in the future.

Turning to the national economic picture, Mr. Deming noted that the spring season had brought with it widely quoted statements of economic upturn which appeared to be based on solid statictical evidence. It was difficult, however, to characterize the upturn prospects fo far as much better than "sluggish," or to see any signs of significantly lower levels of unemployment.

Mr. Deming expressed the view that credit policy should continue pretty much on an "as is" basis, with a slight leaning toward more ease. It should be possible to accomplish this successfully, he felt, even with the Treasury in the market with tax bills, an increase in the amount of regular bills, and refunding of annual bills. He saw no great danger in a slightly easier policy, not even much danger that short rates would weaken, and he did not believe the System would be pressing so much liquidity upon the banking system as to cause trouble in the future. In fact, as mentioned earlier, bank liquidity at present seemed to him to be short rather than ample. In more precise terms, he would be inclined now to return to bank reserves as a primary policy guide, obviously tempering policy if short rates showed signs of weakening significantly. He would try to keep free reserves between $500-$600 million and total reserves about in keeping with the needs indicated by the Board staff table. He saw no need to change the discount rate or the directive at this time.

Mr. Allen reported that in the Seventh District there was growing confidence, based on a number of factors, that a low point had been reached and that a gradual upturn could be expected. Unemployment, although heavy, did not seem to be rising further; the strongest labor markets were in those cities producing farm machinery or otherwise oriented toward the farm economy, while the weakest were those influenced by automotive production. The recent improvement in sales and production of farm machinery was expected to continue. Sales of automobiles had also improved, but they were still well below last year. While production schedules were being increased, production would doubtless continue to run well below last year. Current estimates from Detroit were that production for the first quarter would approximate 1,184,000 units, and that second quarter production would be 1,370,000 units, or 24 per cent below the 1,807,000 produced in the second quarter of last year.

Steel production was holding steady at the moderately improved level of late February. Although steel producers in the area had experienced no vigorous pickup in orders, they were pleased with the order trend, which showed some improvement in orders from most types of customers, and they felt that the decline in auto industry orders would be reversed in the second quarter. Also, in recent weeks trucking lines and railroads had found their "miscellaneous" (general merchandise) loadings rising, indicating to their analysts that some firms which had been cutting inventories were beginning to order additional supplies. The trend was modest, but it appeared significant because it was quite general. Department store sales in the four weeks ending March 18 were 6 per cent above last year in the District. The earlier Easter was undoubtedly a factor, but it did not entirely account for the improvement.

Judging from data supplied by weekly reporting District banks, business demand for credit had strengthened in the past few weeks. This could be ascribed in part to the failure of dealers and processors of farm products to pay down borrowing seasonally. Special conditions in the markets for cotton and soybeans had led to some speculative buying, as well as higher prices, and had boosted financing requirements. Therefore, although it might be premature to assume that the cyclical low in demand for credit had been passed, it seemed clear that a pattern of heavy liquidation such as obtained from October through January no longer was being followed.

The large Chicago banks had been acquiring Treasury bills, as usual, in anticipation of the April 1 tax date. Although their acquisitions this year were larger than usual, their indebtedness was smaller than in other years. They had been buying Federal funds but had not used the discount window for several periods. It was anticipated that they would do so this week and next.

Mr. Allen said it seemed important that the Federal Reserve, as a professed practitioner of a flexible monetary policy, give timely evidence in its operations of its sense of the business situation. The System was widely credited with having done that a year ago when it moved to a posture of ease. In his judgment the System should reduce the degree of ease in some degree when it believed that an upturn has begun, among other reasons lest substance be given to the claim that monetary policy under the System's direction had an inflationary bias. Hindsight might in the future indicate that as of the present date the economy was definitely in a period of recovery. However, in the light of unemployment and the fact that any upturn, even if the Committee did not sense it, had surely been quite modest, and also in view of current and forthcoming Treasury operations, he would favor continuing for the next three weeks the same degree of ease, the same discount rate, and the same directive, unless it should be decided later in the meeting to alter the form of the directive.

Mr. Clay commented that the moderateness of the national recession had been apparent in the minimal nature of the Tenth District adjustment.

Cyclical adjustments in District general business tend to be comparatively mild, and the developments of 1960-61 provided additional confirmation of that experience. The contrast in cyclical experience in the District relative to the nation was largely explained by the lesser concentration of hard goods industries and by the stabilizing influence of agriculture.

Currently, the trend of nonfarm employment was displaying evidence of renewed strength in several District States. However, business cycle developments were nearly submerged in some local areas by the adjustments resulting from the shifting composition of national defense spending. The reclassification of Wichita and Tulsa into the substantial labor surplus category last week was a case in point. At the same time, other areas in the District were experiencing expanding military production activity.

Except for some local areas, 1960 was a good year for farm income in the District--granting that individual farmers felt the impact of the structural readjustment through which agriculture was moving. Cash receipts from last year's crops, favorable cattle prices, abundant feed supplies, generally favorable moisture conditions, and excellent wheat crop prospects had combined to get 1961 off to a good start in Tenth District agriculture.

On the national scene, Mr. Clay noted that there was further evidence that a turnaround in economic activity might be in the making. He suggested that in furtherance of that development, monetary policy should continue to be directed toward ease. This stage of the cyclical movement appeared to call for such a policy in any case, but the need was underscored by the amount of unemployed resources that would have to be absorbed in the course of recovery. In implementing this policy, the System's open market operations should be conducted with a view to their possible downward pressure on the rates of the longer maturities. While these rates had declined appreciably from the peak of early 1960, they still remained unusually high, as pointed up by the fact that the long-term rate on Treasury securities was now substantially above the low of the 1958 recession and slightly above the peak levels of the 1957 boom. The difficulties encountered in attaining lower long rates under present circumstances should not deter the Committee from pushing its operations in that direction, recognizing that the main effect might be to prevent a premature tightening of the longer end of the market. Some encouragement could be derived from reports of lower residential mortgage rates, portfolio lengthening of some institutional investors, and a strong flow of funds to savings institutions. Mr. Clay considered it unnecessary to take any action designed to move the Treasury bill rate up again. He hoped, however, that the bill rate would go no lower than 2-1/4 per cent.

Mr. Wayne stated that business activity in the Fifth District was marked by the diverse trends that usually indicate a turning point in the business cycle. Scattered figures for March showed a distinct and slightly greater than seasonal improvement over the mixed and slightly weaker conditions revealed by the more comprehensive data for February. As in the

Minneapolis District, a substantial portion of the unemployment was structural and would continue for some time. A small sample of the larger banks in the District showed that they were planning for a consistent rise in loan demand as the year progressed; they had shortened their investment position in recent months so that they were now in a reasonably good position to meet that increased demand. There had been encouraging increases in new orders in several fields such as furniture, lumber, steel, and textiles. This, coupled with the fact that prices were holding firm, made most manufacturers moderately optimistic for the near future. Department store sales were quite good; after allowance for unusual seasonal factors, it was possible that the March index of department store sales for the District might equal or exceed the previous high record.

For the country as a whole, Mr. Wayne said, recent information strengthened his belief, expressed three weeks ago, that the decline had ended. Almost all of the information on March activity showed improvement over the February level, and thus far there had been no news of unfavorable developments in any major sector of the economy. The most significant improvements were the sharply higher sales by department stores, increased automobile sales, plans for expanded production by automobile producers, and reduced claims for unemployment compensation.

The position of banks in the Fifth District was comfortable but somewhat less easy than earlier this year. Holdings of short-term Governments had risen considerably, and time deposits continued to rise.

Mr. Wayne expressed the opinion that in view of the mounting evidence that the recession had reached bottom, and in view of the easy conditions in the money market, it would not be appropriate to move toward more ease at this time. On the other hand, it would certainly not seem wise to tighten credit just as the first signs of a possible recovery had begun to appear. As he saw it, therefore, the logical course to pursue was to continue the present open market policy and to keep discount rates unchanged, at the same time keeping a close eye on the 90-day bill rate.

Mr. Mills said that it seemed desirable for the Committee to redirect its thinking from time to time. At this time he would suggest turning away from some of the more extraneous factors that properly entered into policy deliberations such as the marked improvement in business confidence and the devoted consideration in some quarters to the status of the money supply. What the Committee might preferably do was to turn its thinking back to its fundamental responsibility for determining that there was a credit availability within the commercial banking system sufficient to nourish the economy in its present stage. In other words, the Committee should devote its efforts to providing a credit base that would accommodate the existing and prospective needs for credit throughout the economy. In his opinion, the reserve climate that existed in the past three weeks was appropriate to that objective and also the additional objective of fostering a short-term interest rate consistent with short-term rates in the international sphere of finance. He agreed with Mr.

Hayes that it would be a grave mistake for the System to lower its guard at the present time and to feel that the international situation had become stabilized to a degree that eliminated the responsibility for providing a domestic scene that would be regarded by foreigners as conservative and responsible.

To set up the money supply as a factor that deserved the complete attention of the System in its policy-making, Mr. Mills said, could presumably lead to questioning abroad because, as he understood its proponents, acceptance of such a policy would require exerting determined efforts to increase the money supply as a means of fostering credit expansion. It would seem to him more logical to regard the money supply, and its growth, as an accompaniment of growing demand for bank credit than an element that should be stimulated in the hope that an expanded money supply would of itself permit the growth of credit. At the present time, when there was international foreknowledge that the Federal budget was coming into a deficit and that there would be deficit financing on the part of the Government, there would be good reason for developing a monetary and credit policy that in a sense would act as a counterweight to the expectation that the deficit financing might lay a seed bed for future inflation. In his opinion the policy of the past three weeks had accommodated credit needs and at the same time had permitted stability in the international interest rate structure, both of which were desirable in view of the prospect that the Treasury would be coming to the market for new cash at intervals over the months ahead. There would be adequate opportunities on those occasions to permit at least some part of that financing to be accomplished through the banking system, and in that manner give the support that would be desirable for fostering a growth in the money supply which would come from a credit demand associated with the needs of the Government and not from a policy that would just aim at pumping up the money supply as and of itself.

Mr. Mills said in conclusion that he saw no reason to change the directive or the discount rate at this time.

Mr. Robertson commented that, as the Committee was aware, it had been his view for many months that the Committee had not permitted monetary policy to make the fullest contribution it could toward changing the trend of economic events. This did not mean that the System had not done a good job. It had moderated the recession, but he thought it could have done much more than it did. One of the reasons for the failure to act in the manner that he considered proper was the undue emphasis on the bill rate. Even in the past three weeks, he felt there had been undue concentration on the bill rate, at the expense of injecting enough reserves to permit the money supply to be augmented. There was at least a possibility that the System might be faced within the next few months with an entirely different picture, one in which a posture of restraint would become necessary because of the speed of recovery, and it would be difficult to follow a policy of augmenting the money supply at that time. Therefore, he felt that the System should be acting now and that it should be aiming toward an easier position than at present.

With regard to the current experimentation in longer-term securities, Mr. Robertson said he supposed everyone had been endeavoring to appraise the effect of that experimentation and that everyone might have a different view. Personally, he could not see that much had been gained from the experimentation. He doubted that many would feel that the experiment had gone on long enough to judge whether or not it was possible to tinker successfully with interest rates to the advantage of the economy. However, he saw a possibility that the System might be subjecting itself to a charge in the future that it had entered upon this experiment for show purposes only and had not attempted to make it work. It might be contended, on the other hand, that the System should experiment gingerly to be sure it was not making a mistake, but in his opinion if the System was really going to experiment, it should experiment on a sufficiently large and broad basis to provide proof one way or the other concerning the efficacy and desirability of the operation.

With respect to the comments that had been made this morning about the foreign situation, Mr. Robertson said he felt that this factor had been permitted to dominate the direction of System policy for too long. A comment had been made by Mr. Hayes to the effect that recently there was little indication of foreign interest in the Government securities market, long or short, but that there had been increased interest in the stock market. This might mean that people did not like to play a game if they did not know what rules were being followed. This was one of the difficulties involved in going into the longer-term area.

Mr. Robertson concluded by repeating that in his opinion the Committee ought to be aiming at an easier position. This should not be interpreted, however, to mean that he advocated flooding the market with reserves. To indicate the type of ease of which he was speaking, he would move up free reserves by about $150 million over the next three weeks, irrespective of what that did to the bill rate. He would not amend the directive at this time unless the form of the directive was to be changed.

Mr. Shepardson said that from the standpoint of the domestic situation it seemed to him this was a time for cautious optimism. There were some indications that in the not too distant future conditions might improve, but he questioned how fast that improvement might be. The foreign situation was in his opinion still a significant factor. In the light of both situations--domestic and international--it appeared to him that the System would do well to continue about "as is." To judge by the availability of Federal funds, there had been adequate ease. Also, there had been an increase of savings funds that might be characterized as funds held temporarily in abeyance due to uncertainties. He questioned whether they were long-term savings funds and felt that they could easily become part of the money supply if and when people gained more confidence. However, in view of the domestic situation, the prospective deficit in the Federal budget, and the very uneasy and uncertain international situation, he thought it likely that there was going to be a continued accumulation of these so-called savings funds held temporarily out of the spending stream. In summary, he believed that the degree of ease at the moment was adequate and would favor continuing at about the same level.

Mr. King referred to Mr. Shepardson's comment about cautious optimism and said his own state of mind might be characterized as one of cautious pessimism. With regard to the question whether the degree of monetary ease had been sufficient, he said it was difficult for him to see how, if monetary policy had been too restrictive, it could be suggested that it might contribute to a very rapid recovery. If monetary policy had been too restrictive, he would think that the recovery was more likely to be dull. The current posture of the System seemed to him reasonable; in his opinion, it was about as helpful and as good for the general economy as any policy that could be developed. Actually, the System had been pursuing quite an easy policy for some time, the only indication of restraint having been that associated with the maintenance of the bill rate. As to the bill rate, it was his hope that it would continue to be regarded as a significant factor in the future, at least during the next few weeks. He considered the present level preferable to the level of three weeks ago, and he hoped that the bill rate could stay in the present range, varying not too much in one direction or the other. As to free reserves, he felt that a level somewhere around $600 million would be appropriate. A comment had been made earlier that perhaps the time had come when the level of free reserves should again be regarded as a more important policy guide, but he did not see how that was possible as yet. He expected that free reserves might fluctuate rather widely within the range of $500-$700 million. In general, however, he would hope that the present degree of ease and the present tone of the market might continue for some time.

Mr. King suggested that the directive might be amended at the appropriate time simply to provide for fostering recovery rather than for encouraging monetary expansion for the purpose of fostering sustainable growth in economic activity and employment. He believed that such language would permit the System to operate flexibly and that there was some danger of misunderstanding in the protracted use of the phrase "encouraging monetary expansion." Mr. Swan, he noted, had suggested that before long it might be too late for such a change to be appropriate. As he saw it, however, it might not be reasonable to start "encouraging recovery" until there was evidence that the recession actually had bottomed out. In his view, therefore, it might only now be appropriate to make a change of that kind. On the other hand, he did not feel strongly about the matter.

Mr. King said he saw no occasion for a change in the discount rate. If open market operations could continue to be conducted along about the same lines as in the past three weeks and if the same general tone could be maintained in the market, he would be well satisfied.

Mr. Hilkert reported that like the country as a whole, the Third District seemed to be moving along the bottom of the recession. Three weeks ago the indicators hinted at this. Now they had improved further, and the signs appeared fairly consistently in the various sectors of the economy--in production, labor markets, and consumption. The new index of electric power consumption by manufacturing concerns showed an increase, seasonally adjusted, in January and again in February--the first two-month increase since early in 1960. Furthermore, the increase was concentrated in durable goods industries. Steel production was up, along with carloadings. Unemployment claims were declining, and in February manufacturing employment picked up in several of the District's labor market areas. Department store sales had increased substantially, and only part of this was attributable to the earlier date of Easter this year.

The banking picture had changed little since the end of January. Although some decline is usual at this time of year, bank credit had shown considerable strength. Loans and investments at reporting banks had declined since the last Committee meeting, but total deposits of all

District banks had increased, and by a larger amount than in the comparable period last year.

Mr. Hilkert commented that in view of current Treasury financing operations, any significant departure from recent policies would not be in order. Even aside from considerations of Treasury financing, however, it seemed to him that it would be appropriate to continue the same degree of ease. The economy had only bottomed out at best, and it was still far from certain how strong and rapid the recovery might be. Interest rates already were higher for this phase of the cycle than in other postwar recessions, and with recovery on the horizon, pressures would seem to be on the side of still higher rates. For this reason, it would seem desirable to continue to supply reserve needs mainly by purchases of intermediate and long-term securities. If the volume of purchases necessary to prevent any significant rise in intermediate and long-term rates resulted in some increase in free reserves, he would not be disturbed. He would make no change in the directive or the discount rate.

Mr. Bryan said that the situation in the Sixth District differed only as to details from the situation reported in other districts and nationally, and that he did not believe it was necessary to recite those details at this time. As to the situation nationally, he agreed with nearly everything that had been said. His own judgment was that the bottom of the recession was very near, if not already at hand, thus leaving the System with the problem of trying to determine whether there would be a slow recovery of the kind that had followed some recessions or a sharp recovery of the kind that had occurred in other cases. He did not care to venture a prediction in that respect. However, on the matter of how far the System should go in trying to nourish recovery, he brought out that at times in the past the System had been subject to criticism--and he thought with some cause--on the ground that it had overstayed its position of ease in the recovery stage and then finally clamped down rather abruptly.

At the moment, Mr. Bryan said, he found himself quite pleased with the reserve position. On the Board's seasonally adjusted series, total reserves were almost exactly on the long-term trend line, and other figures were in about the same shape. Therefore, he found himself leaning toward the position expressed by those who had suggested that the System should move cautiously in providing any further ease. Thus, for the next three weeks he favored a policy of supplying or absorbing reserves in an amount adequate to cover the usual seasonal variation, plus something to allow for necessary growth in the economy. Moreover, as he saw it, the System should move cautiously not only in that respect but in some other matters such as short-term rates. However, he would prefer to withhold any detailed comment on those matters.

Mr. Johns said there was almost nothing in the Eighth District situation that seemed to warrant specific comment at this time. The employment and unemployment statistics were rather perplexing, particularly in the St. Louis area, because of the fluctuations occasioned by intermittent shutdowns at automobile assemply plants. Eliminating that factor, the situation in the District was about in line with the national picture in terms of employment and unemployment as well as in other respects.

Mr. Johns said he continued to believe, as he did three weeks ago, that in the present situation the policy directive, which called for encouragement of monetary expansion, was appropriate. He had no strong feeling as to whether clause (b) should provide for fostering sustainable growth in economic activity and employment or for fostering recovery; if the System fostered sustainable growth it would also be fostering recovery. However, he would like to see compliance with the directive insofar as it called for continued encouragement of monetary expansion. He would hope that the Committee could gradually recover the deficiency in actual reserves, as shown in the memorandum from the Board's staff, and do a little better than the projections set forth in Table 2 of the staff memorandum. He would not favor a change in the discount rate at this time.

Mr. Szymczak said that he would favor no change in monetary policy. He felt that the Desk was doing an excellent job, and he hoped the Committee would continue to do everything possible to prevent the short-term rate from going down.

Mr. Balderston presented the following statement:

> In the second and third quarters of 1958, the three months' moving average of annual rates of money supply growth rose to between 3 and 5 per cent.

With the disappearance of free reserves at the end of 1958, the rate of money supply growth slackened, and after a lag of seven months became negative.

When free reserves climbed between the last half of 1959 and early 1961 to over $600 million, the money supply growth rate responded and after the middle of 1960, changed from negative to positive.

After the first half of this past February, however, the money supply growth rate fell and since February has been at a standstill. In fact, the money supply, in absolute terms, is currently about the same as in the last half of October.

Conclusion: With the gold outflow stopped, at least for the moment, it seems that the Committee should experiment with free reserves of $600 million or more until the money supply responds. In 1958, $500 million of free reserves induced a 3 to 5 per cent annual rate of money growth. Now, with the counting of vault cash, the free reserve figure required to make the money supply respond seems to be higher than in 1958. How much higher can be determined only by probing, which in my view should start at once.

While this probing is under way, the bill rate is likely to decline despite significant help from the increased supply of bills being offered by the Treasury. Although I would not wish to see the bill rate below 2 per cent, or 1-1/2 per cent at the very minimum, the differential rate advantage of London has disappeared for the time being and the pound rather than the dollar is under pressure. It would be a pity if a lowered bill rate were to be interpreted as an indication that this country's balance-of-payments problem is solved, and the Committee should continue to employ devices to avoid depressing the rate by heavy buying of bills. However, the time seems to have arrived to risk some decline in the bill rate and to resume the stimulation of money supply growth. If the cyclical bottom has been reached already, the economy should be prepared to put additional reserves to constructive use.

Prior to the presentation of this statement, Mr. Balderston had distributed copies of a chart portraying the relationship between the bank reserve position and the active money supply over the period 1953-61. 1/

1/ A copy is attached to these minutes.

This chart, he said, had been developed for him by Mr. Eckert of the Board's staff. In further comments, Mr. Balderston explained that he was seeking the answer to the question often posed by Mr. Thomas; that is, the level of free reserves that is necessary to cause the money supply to continue to rise. He was unhappy about the fact that the money supply had not risen since early February, and he was no longer willing to console himself with the fact that time deposits had been rising at a rapid rate. There was a secular trend in time deposits that would cause them to rise anyhow.

Chairman Martin said that in his opinion the balance-of-payments problem was not being exaggerated. Domestic economic recovery might be under way, or it might not be, but in any event he was apprehensive that the balance-of-payments problem would be increased rather than resolved by the recovery. It seemed to him that the wage-cost spiral had reached the point where, if it was ignored and recovery developed, the temporary improvement in the gold situation could reverse itself quickly. Accordingly, it was his opinion that the problem was an extremely serious one.

As to the current position of the domestic economy, Chairman Martin said he could not help but look at the situation from a longer-range point of view. In that perspective, he wondered whether the current period actually represented anything more than a wrinkle in the 1958-59 recovery from the preceding recession, rather than a serious business decline or recession. Assuming that the economy was now at the bottom of the current recession--and he did not want to say whether this was actually the case--it should be noted that the decline had been moderate; the industrial production index had fallen only from 111 to 102. Thinking of the events that led up to the 1957-58 recession, including the excesses that occurred and the time bomb resulting from the end of the war and the accompanying inflationary forces, it might well be that in looking at the chart at a later date one would conclude that the current recession was only a slight wrinkle in a sustained upswing. For this reason, he did not think it material whether one talked of "fostering recovery" or about an adjustment process in the economy preceding an upward movement. It seemed to him that the System had done surprisingly well in a period of great difficulty.

Turning to the recent operations of the Open Market Account in longer-term securities, as authorized at the February 7 meeting, Chairman Martin noted that one financial writer had already concluded that these operations could be labeled a failure. Personally, he did not know how one could make a judgment within the space of only about five weeks. Mr. Robertson had pointed that up well when he said that no one could hope to find proof one way or the other in such a short period. As to the view that the results of the experimentation could be proved one way or the other by dramatic action in the market in a given period of time, he (Chairman Martin) was afraid the problem was not that easy.

It must be recognized, the Chairman said, that there might be some fundamental changes in the Government securities market. To emphasize this, he would only reiterate his opinion that if there should be another situation such as developed in 1958, when the 2-5/8 per cent Treasury bonds fluctuated in price more than common stocks, one could not expect the Government securities market to be continued in its present form. There had been the Treasury-Federal Reserve study of the Government securities market, started in the spring of 1959, and many different views would be expressed on how the market ought to be organized, or reorganized. Thus, the matter was in a transition stage at this time.

The Chairman then commented that the Ad Hoc Subcommittee that had been looking into the Committee's operating procedures held another meeting yesterday afternoon. After discussion, the Subcommittee came to the unanimous view that it was too early to try to decide on a revision of the Committee's operating policies and that it would be desirable to take more time. Probably the Committee ought to consider in due course a division of the directive to put it in more orderly form, but the operating policies had been in effect for a long period of time. Recently they were modified by the February 7 authorization to operate in longer-term securities, and public notice of this modification had been given by the statement issued by the Manager of the Account on February 20, 1961, at his (Chairman Martin's) direction and with the Manager's full concurrence. Thus, with one exception, the Committee had now untied its hands completely.

This exception was the limitation of 10 years on the maturity of securities in which the Account Manager was authorized to conduct operations. The Manager was not particularly anxious to do too much in the area beyond 10 years, but the Subcommittee felt that the Manager's hands probably should not be tied even to that extent.

In the circumstances, Chairman Martin suggested that it might be well for the Committee to consider today a renewal of the special authorization given on February 7, and renewed on March 7, but in doing so to give the Manager of the Account freedom to operate in all maturities. This would give the Committee more time to look at the problem before coming to grips with the kind of directive that it wanted to write.

Continuing, the Chairman commented that some people might feel that the System had not made a bona fide effort in its experimentation in operations in longer-term securities because it had not acted more aggressively. On the other hand, some people felt that the System had acted too aggressively. He had found market opinion divided, some saying that the System's operations had dried up and undermined the market while others said that the market already was beginning to improve. He did not know how to appraise those opinions, but he had talked with competent people and had gotten conflicting views.

Chairman Martin expressed the view that to let the bill rate go down to 1-1/2 per cent would invite disaster. Such a move would call for a reduction in the discount rate, and the problem with respect to foreign markets would be compounded. As he saw it, the whole problem was one of not getting too far out of line on interest rates. Should the bill rate drop substantially, the Bank of England, for example, might feel that it had to make an adjustment. It must be remembered that countries abroad were facing inflationary problems.

In his opinion, the Chairman said, the Committee should give the Manager as much leeway as possible. It should not bind itself to any fixed level of free reserves. He felt the System had been operating quite well recently, and it should continue to try to keep the short-term rate from taking a dive. All one had to do was to look at the market to know that it was easy; Federal funds were practically going begging periodically. If the System was going to try to prime the pump to force the money supply statistics up, it might only create a sloppy situation which would be difficult to correct.

Chairman Martin said he did not know exactly how to pull together a meeting of this kind because there appeared to be some rather broad differences of opinion. However, he would first put up for consideration the unanimous recommendation of the Ad Hoc Subcommittee, which reflected a motion made by Mr. Mills and seconded by Mr. Irons. The recommendation was that consideration of a revision of the Committee's three statements of operating policies again be tabled and that, pending their later consideration, the Committee continue to operate as at present, except that the restriction on the special authorization for the Account Manager to operate in maturities only up to 10 years be eliminated. In this connection, the Chairman also noted that Mr. Rouse had some question about the use of the go-around technique when operating in longer-term securities, as indicated by the latter's comments today. There were also some differences of opinion on that point within the Ad Hoc Subcommittee. Even there, however, it was recognized that if the Open Market Committee was going to be able to make any appraisal at all, it must have some experience on the basis of which to reach judgments.

There ensued a colloquy between the Chairman and Mr. Balderston regarding the policy envisaged by the statement that the latter had presented, and Mr. Balderston stated that essentially his recommendation was to probe toward a level of free reserves of $600 million or more. While he did not want to see the bill rate go down, if the Committee was going to force an increase in the money supply by an increase in the amount of free reserves, other forces in the market might be such that the bill rate would have to go below 2 per cent. At that point he would be concerned, just as he was in June 1958 when the bill rate fell below 1 per cent. For the past several months, he noted, it had been necessary to take time out to fight the outflow of gold. He did not think that the problems that had caused the gold outflow had been corrected, but now that the outflow had stopped for the moment he felt that the System should pay attention once more to the money supply. As indicated by the directive, encouragement of monetary expansion was one of the objectives of System policy.

The Chairman then said that apparently he had misunderstood the nature of Mr. Balderston's recommendation. It now appeared that the difference in thinking was principally between aiming at a level of free reserves of $400-$500 million or a level of $600-$700 million.

Turning to the policy directive, the Chairman stated that as he understood it the consensus was against changing the directive at this time.

Mr. Irons observed that normally the Committee had followed the practice of changing the wording of the directive coincident with some basic change in policy, usually at some turning point of the business cycle. He inquired whether a change in the wording of clause (b) to call for "fostering recovery," as had been suggested, would involve merely a matter of semantics, or whether it would infer a basic change in policy. He was not ready for the latter.

Chairman Martin replied that this question illustrated the basic difficulty. The point had been made that it might soon be too late, if it was not too late already, to adjust the directive so as to provide for fostering recovery. However, another Committee member had made the point that recovery actually started only when the recession had bottomed out. The consensus today appeared to be against any change in open market policy; as Mr. Irons had indicated, it was customary to change the wording of the directive only when the Committee was changing policy. Therefore, on the basis of past practice, there would seem to be a case against making any change in the directive at this time.

In further discussion, several members of the Committee indicated that they did not favor a change in the directive in the current circumstances.

Mr. Shepardson suggested that a mere change in words might be misleading, since the consensus today was against any signficant change in open market policy.

The Chairman inquired whether anyone felt that the consensus today was not as stated by Mr. Shepardson, and no comments were heard. Accordingly, the Chairman said that this would be taken as the consensus. He next inquired whether anyone felt strongly enough about a change in the directive to want to record a vote to such effect, and again no comments were heard.

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

(1) To make such purchases, sales, or exchanges (including replacement of maturing securities, and allowing maturities to run off without replacement) for the System Open Market Account in the open market or, in the case of maturing securities, by direct exchange with the Treasury, as may be necessary in the light of current and prospective economic conditions and the general credit situation of the country, with a view (a) to relating the supply of funds in the market to the needs of commerce and business, (b) to encouraging monetary expansion for the purpose of fostering sustainable growth in economic activity and employment, while taking into consideration current international developments, 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.

Mr. Robertson inquired concerning the proposed implementation of the directive over the next three weeks, and Chairman Martin said he understood that open market operations would be guided by the consensus, which, as had previously been agreed, favored no change in existing policy.

Mr. Robertson then said that he would like to be recorded as dissenting from such implementation of the directive because, although he had voted for renewal of the directive, he did not agree that the existing open market policy represented a proper implementation of the directive.

Secretary's Note: Mr. Robertson subsequently submitted the following statement for inclusion in the record of the meeting in explanation of his dissent:

Mr. Robertson dissented from the decision to maintain, until the next meeting, the existing degree of ease. At the past several meetings, as at this one, he had voted to approve the current directive, on the ground that it correctly specified that open market operations should be conducted with the aim of "encouraging monetary expansion." However, in the last few months the degree of ease which he thought appropriate to achieve the aim of the directive, and which he thought had been sought by the Committee, was not reached--principally, in his opinion, because too much emphasis had been attached to seeking to prevent a reduction in the interest rate (i.e., yield) on short-term Government bills. Consequently, in his view monetary policy had been precluded from making its full contribution to a reversal of the economic downtrend.

> Now that the gold outflow had abated, he believed there was even less reason that heretofore to gear open market action to the maintenance of a particular bill rate rather than to the provision of what he would think were sufficient bank reserves to stimulate business activity and economic growth, and thus contribute to the solution of the serious economic problems that arise from failure to utilize fully our human and material resources. Believing as he did that the supply of bank reserves should be increased in an amount sufficient to encourage monetary expansion and thereby to promote economic recovery, at a time when there was little danger of reviving inflationary pressures by such further monetary ease as he sought, he deemed the proposed policy decision inadequate to meet the needs of the time.

Mr. Balderston stated that he also would like to be recorded as dissenting from the consensus as to implementation of the directive because he felt, for the reasons indicated in the statement he had made earlier, that it would be desirable to probe toward free reserves of around $600-$650 million.

Mr. Swan likewise indicated that he would dissent from the decision on implementation of the directive on the ground that, as he understood it, that decision would not contemplate probing toward the level of free reserves mentioned by Mr. Balderston.

Mr. Ellis stated that if he were a member of the Committee he would dissent on the same basis as Mr. Swan. Mr. Johns indicated that if he were a member he also would dissent because he would favor being a little easier than envisaged by continuation of the existing policy.

Accordingly, it was understood that Messrs. Balderston, Robertson, and Swan dissented from the majority decision that until the next meeting of the Committee the policy directive, as approved by unanimous vote, would be implemented by open market operations seeking to maintain about the existing degree of ease in the reserve position of banks. It was understood that Messrs. Ellis and Johns, not at present members of the Committee, also dissented.

Chairman Martin then referred again to the recommendation of the Ad Hoc Subcommittee. This recommendation, as previously stated, was that the special authorization for operations in longer-term Government securities which was given by the Committee on February 7, 1961, and renewed on March 7 be changed to remove the restriction against operations in securities having a maturity longer than 10 years. The recommendation of the Subcommittee also contemplated tabling further consideration of any change in the Committee's operating policies, which meant that the Committee would proceed for the time being in the light of the policy directive to the Federal Reserve Bank of New York, as supplemented by the special authorization to engage in operations in longer-term securities. The special authorization, in the form in which it would stand following the proposed amendment, was as follows:

> The Committee authorizes the Federal Reserve Bank of New York, between March 28, 1961, and the next meeting of the Committee, within the terms and limitations of the directive issued at this meeting, to acquire intermediate and/or longer-term U. S. Government securities, or to change the holdings of such securities, by an amount not to exceed $500 million.

Mr. Allen said he regretted that the Ad Hoc Subcommittee could not have presented a recommendation at this time for a change in the statements of the Committee's operating policies. He understood the difficulty and did not mean to be critical. The reason he regretted the lack of a recommendation was that he did not like to have to voice disapproval at each meeting concerning the areas of the market in which operations for the Account were now authorized. He would like to get that matter out of the way. He still felt as he had expressed himself at the February 7 and March 7 meetings about extending Open Market Account operations to longer-term securities. However, since the majority of the Committee had chosen to authorize such operations, he was in agreement with the recommendation of the Subcommittee that the restriction against operations in maturities beyond 10 years be removed from the special authorization.

Mr. Robertson said that he would want to be recorded as dissenting from the proposal to remove the 10-year maturity limitation on securities covered by the special authorization because the recommendation involved continuing the authority to engage in operations in other than short-term securities. For the reasons he had stated at the February 7 meeting and reiterated on March 7, he was opposed to the granting of such authority. In essence, his reasons were that he considered the authorization inappropriate and that the Account Manager was given no guide for operations in the longer-term area.

Mr. Bryan said that if he were a member of the Committee he would vote to approve the recommendation of the Ad Hoc Subcommittee that the restriction against operations in maturities beyond 10 years be removed. However, he had sympathy with the view expressed by Mr. Robertson. He would approve the recommendation only because he felt that if the Committee was going to experiment it might just as well experiment boldly.

Thereupon, the Committee authorized the Federal Reserve Bank of New York, between March 28, 1961, and the next meeting of the Committee, within the terms and limitations of the directive issued at this meeting, to acquire intermediate and/or longer-term United States Government securities of any maturity, or to change the holdings of such securities, in an amount not to exceed $500 million.

Votes for this action: Messrs. Martin, Hayes, Balderston, Irons, King, Mills, Shepardson, Swan, Szymczak, and Wayne. Votes against this action: Messrs. Allen and Robertson.

Mr. Allen's vote was subject to the understanding that since the authorization to operate in longer-term securities was being continued in effect by majority vote, he would not object to removal of the restriction against operating in maturities beyond 10 years.

Secretary's Note: Mr. Robertson subsequently submitted the following statement for inclusion in the record of the meeting in explanation of his dissent:

Mr. Robertson expressed at the February 7, 1961, meeting his reasons for dissenting from the proposal to carry on open market operations in other than short-term Government securities. He now dissented from action to expand the original proposal by authorizing the Manager of the Account to buy and sell securities having maturities exceeding ten years, not only on the basis of

> his conviction that the whole operation was unwise, the risks being too great to be offset or counterbalanced by all the alleged potential benefits, but also because this proposal represented a further delegation of authority from the Committee to the Manager of the Account <u>without any plan or program to guide him in his operations</u>. He did not believe the Manager could be expected to carry out the Committee's unspecified objectives--whatever they were--solely on the basis of his own intuition.

With regard to the earlier reference by Chairman Martin to the possibility of changes in the Government securities market, Mr. Rouse said he would like to comment along the same lines. The speculation in rights in 1958 was only a facet of a larger problem affecting the whole bond market. The price swings of the past 10 years, in two or three cycles, had reached the point where, if they continued, there was not going to be any bond market. They were wide enough to drive people out of the bond market and into the stock market or other forms of investment, and they had brought a large speculative element into the Government securities market. This problem was something that deserved serious consideration on the part of the Open Market Committee because the System plays a significant role in the market climate in which the swings in prices and rates occur. The swings could not continue to be as wide as they had been if there was going to continue to be a bond market, Government, corporate, or municipal.

Mr. Rouse then turned to the general instructions that he considered had been given by the Committee to the Manager of the Open Market Account, particularly with respect to the experiment--or whatever it might be called--in operating in longer-term securities. In this connection, incidentally, he hoped that the word "experiment" would not be used in talking with outside parties for, as he had said at the February 7 meeting, the use of that word had a tendency to kill the effect of the operations. As he saw it, there were two things involved. One was the insertion and withdrawal of reserves in an area of the market that the System had not used for many years, in order to see whether that was a feasible operation in relation to the market. Then there was the secondary item, which involved rates. The Committee had regarded the short-term rate with a great deal of concern; therefore, some of the Desk's efforts had been devoted to keeping the short-term rate from going below 2 per cent, and preferably keeping that rate in the area that it had been in for the past several weeks. In addition, to the extent that the insertion or withdrawal of reserves had had, or might have, an effect on longer-term rates, that was a factor to be considered in operations for the System Account. Mr. Rouse said his interpretation of the general instruction was that the System was not trying aggressively to bring down longer-term rates, but that this was in passive terms. However, if they did come down as a by-product of operating in the longer-term area, that was something the Committee would consider desirable. The removal from the special authorization of the restriction against operations in maturities beyond 10 years did not suggest to him active participation in the long-term area of the market in an aggressive sense, although the Desk ought to be active enough to indicate a degree of flexibility. In this area the New York Bank had on hand orders from the Treasury for trust funds or other funds that were endeavoring to get into higher-yielding securities. However, this was primarily an investment operation, rather than an experimental operation in driving down interest rates.

Mr. Robertson asked whether the Committee had contemplated that the experimentation in the longer-term area was to be passive, or an active effort to push down longer-term rates while holding up short-term rates.

Chairman Martin replied that he thought he agreed completely with Mr. Rouse on that point. The Committee did not intend to change monetary policy by authorizing a change in operating techniques, and it did not intend to make interest rates the sole criterion. The Committee had earlier stated in its operating policies that transactions for the System Account in the open market were to be entered into solely for the purpose of providing or absorbing reserves. However, in providing or absorbing reserves, the System does exert an effect on interest rates. The techniques by which the System deals in the market and the way in which the Treasury issues securities have some impact on interest rates. As pointed out in his recent statement before the Joint Economic Committee, the Chairman said, he did not know whether a meaningful change could be developed as a by-product of System operations in longer-term areas of the market. In any event, he was sure the Committee did not intend to shift the whole fulcrum of monetary policy from the providing and absorbing of reserves to interest rates.

Mr. Robertson said he appreciated this point. However, he had thought that the comments of members of the Committee, and also certain statements of persons connected with the Administration, had referred to twin objectives; namely, making money available at lower cost for mortgages and so forth, and holding up short-term rates. Now it appeared that the Committee wanted to be passive in operating in the longer-term area.

Mr. Hayes indicated that his thinking differed a little in degree from that expressed by Mr. Rouse. The Committee had as its major objective the maintenance of a certain type of credit policy; that is, one of moderate ease. Although this was hard to measure statistically, it probably involved maintaining some reasonable kind of reserve position for the commercial banking system. However, he saw no reason why the Committee could not have at the same time the aforementioned objective of monetary ease, the objective of not permitting the short-term rate to go too low, and also the objective of trying to exert some positive effect on longer-term rates. In his mind, the Committee had all of those objectives. There were limits in terms of the market in pressing too hard on any one of these things, but the Committee could recognize all the objectives. He did not feel that one could draw a clear line between an active and a passive approach in the longer-term area.

Mr. Robertson commented that this was a good illustration of how unfair the Committee had been to the Manager of the Account. He questioned how the Manager could be expected to carry out the views of the Committee when they appeared to be so varied. He thought Mr. Hayes was correct in feeling that the Committee had intended to affect the longer-term rates. However, he did not think the Manager should be asked to carry out the will of the Committee unless given more specific guidelines.

Mr. Mills said that, to paraphrase what the Chairman had said, he believed that the recent change in the Committee's operating policies involved a matter of techniques. The effect of the special authorization was to permit the Manager of the Account, within the context and limitations of the broad outlines of monetary policy, to throw the weight of transactions undertaken for the Account on some occasions toward the long end of the market and on other occasions toward the short end, with the prospect that the weight of those transactions might exert some influence either on the long-term or the short-term rate.

Mr. Shepardson commented that this, however, was without any objective of attaining a specific rate.

Mr. Mills said he did not believe that anyone had the concept of a fixed rate, and Mr. Hayes agreed.

Mr. Swan suggested that, although this might be stating the matter in too elementary a fashion, the expression "active", as opposed to "passive", seemed to be related to whether the System was or was not supplying or absorbing reserves at any particular time. Chairman Martin noted that the use of certain techniques in carrying out operations directed at an objective could have by-product effects at times.

Mr. Rouse then said that in the period immediately ahead the Account would be putting reserves into the market, and that would be done in the manner he had described. Then there would be a period when there probably would be no occasion to inject reserves. However, for the sake of continuity, and having in mind continuing pressure on short-term rates, he contemplated that there would be offsetting operations; that is, selling short and buying long. To the extent that those offsetting operations might affect longer-term rates, there would be a desirable by-product.

Mr. Hayes said that he would consider that the transactions Mr. Rouse was depicting would constitute an active role. Mr. Deming commented that the Committee had given an explicit instruction that it did not want the short-term rate to fall too far. In fact, the Committee had talked in terms of a rather specific range. As to the longer-term area, however, the Committee had treated this more or less as a by-product. If there could be some lowering of those rates, that would be desirable. There was no reason not to push down longer-term rates in the course of Account operations, but operations were designed more specifically with a view to their effect on the short-term than the long-term area.

Mr. Hayes said he had not meant to imply that the three objectives to which he had referred earlier were necessarily of equal importance.

Of the three, he would agree with Mr. Deming that the objective of least importance was the lowering of the long-term rate. If a consensus of the Committee were taken, he felt that probably it would indicate a view that the most important objective was the maintenance of a moderate degree of ease. At some times, however, the short-term rate probably was regarded by at least some of the members of the Committee as having as much importance.

Mr. Rouse stated his understanding that the primary objective of the Committee in authorizing operations in the longer-term area was to learn by experimentation over, he would say, a matter of months whether it was feasible for the System to operate in the whole range of the Government securities market rather than in one limited segment of that market.

Mr. Robertson replied that he felt all of the conversation today would indicate that the real reason for operating in the longer-term market was to affect interest rates--whether one spoke of pegging, holding, or reducing--rather than to provide the reserves necessary to meet the needs of the economy. In other words, he felt that the emphasis was on interest rates rather than reserves.

Chairman Martin indicated that he would not agree with that statement. He added that the complexity of the problem could be seen in the words that had been used. Words mean different things to different people, he noted, and he doubted that a useful purpose would be served by further discussion of this particular point at this time.

It was agreed that the next meeting of the Federal Open Market Committee would be held on Tuesday, April 18, 1961.

Chairman Martin noted that Mr. Young, who had been serving as a member of the Treasury-Federal Reserve Steering Committee for Study of the Government Securities Market, had been appointed Director of the Board's Division of International Finance, in addition to continuing as Adviser to the Board. In the circumstances, the Chairman suggested that Mr. Koch, Adviser, Division of Research and Statistics, Board of Governors, be named to succeed Mr. Young as a member of the Steering Committee.

There was unanimous agreement with this suggestion.

The meeting then adjourned.

Ralph A. Young

Secretary

BANK RESERVE POSITION AND GROWTH RATE OF ACTIVE MONEY SUPPLY