MEMORANDUM OF DISCUSSION

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, D. C., on Tuesday, August 15, 1967, at 9:30 a.m.

PRESENT: Mr. Robertson, presiding
Mr. Brimmer
Mr. Daane
Mr. Maisel
Mr. Mitchell
Mr. Scanlon
Mr. Sherrill
Mr. Swan
Mr. Ellis, Alternate for Mr. Wayne
Mr. Patterson, Alternate for Mr. Francis
Mr. Treiber, Alternate for Mr. Hayes

Messrs. Hickman and Galusha, Alternate Members of the Federal Open Market Committee

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

Mr. Sherman, Assistant Secretary
Mr. Kenyon, Assistant Secretary
Mr. Broida, Assistant Secretary
Mr. Molony, Assistant Secretary
Mr. Hackley, General Counsel
Mr. Brill, Economist
Messrs. Jones, Partee, and Solomon, Associate Economists
Mr. Holmes, Manager, System Open Market Account
Mr. Coombs, Special Manager, System Open Market Account

Mr. Fauver, Assistant to the Board of Governors
Mr. Reynolds, Adviser, Division of International Finance, Board of Governors
Mr. Axilrod, Associate Adviser, Division of Research and Statistics, Board of Governors
Mr. Weiner, Assistant to the Director, Division of Research and Statistics, Board of Governors

Mr. Bernard, Economist, Government Finance Section, Division of Research and Statistics, Board of Governors
Miss Eaton, General Assistant, Office of the Secretary, Board of Governors
Miss McWhirter, Analyst, Office of the Secretary, Board of Governors

Messrs. Heflin and Lewis, First Vice Presidents of the Federal Reserve Banks of Richmond and St. Louis, respectively
Messrs. Eisenmenger, Link, Mann, Parthemos, Taylor, Moffatt, Tow, and Green, Vice Presidents of the Federal Reserve Banks of Boston, New York, Cleveland, Richmond, Atlanta, Chicago, Kansas City, and Dallas, respectively
Mr. Lynn, Director of Research, Federal Reserve Bank of San Francisco
Mr. Geng, Manager, Securities Department, Federal Reserve Bank of New York
Mr. Gustus, Research Officer and Economist, Federal Reserve Bank of Philadelphia
Mr. Kareken, Consultant, Federal Reserve Bank of Minneapolis

Mr. Sherman called the meeting to order, noting that in the absence of both the Chairman and Vice Chairman of the Committee the first order of business was to elect an Acting Chairman.

By unanimous vote, Mr. Robertson was elected to serve as Acting Chairman for the meeting.

Mr. Robertson then asked whether there were any comments or suggestions with respect to the draft minutes of actions for the July 18, 1967 meeting of the Committee that had been distributed by the Secretariat on August 10, 1967.

Mr. Mitchell observed that the draft minutes did not include reference to the Committee's authorization for the Special Manager to begin negotiations looking toward placing all of the System's swap arrangements on a twelve-month maturity basis with maturities at year end. In a discussion of the matter he had had with a member of the Committee's Secretariat the latter had noted that any change in the maturity of individual swap arrangements would require Committee approval, whereas on July 18 the Committee had only authorized negotiations that might lead to such actions. However, he (Mr. Mitchell) continued to feel that the instructions to the Special Manager involved a decision that should be recorded in the minutes.

Mr. Robertson suggested that, if there were no objection, the following paragraph be added to the minutes in question: "With Mr. Mitchell dissenting, the Special Manager of the System Open Market Account was authorized to explore the possibility of placing all of the System's swap arrangements on a twelve-month basis, with maturities at year end." No objections were raised.

By unanimous vote, the minutes of actions taken at the meeting of the Federal Open Market Committee held on July 18, 1967, were approved.

The memorandum of discussion for the meeting of the Federal Open Market Committee held on July 18, 1967, was accepted.

By unanimous vote, the action of members of the Federal Open Market Committee on August 4, 1967, approving renewal of the $400 million swap arrangement with the German Federal Bank from August 9 to December 15, 1967, was ratified.

Before this meeting there had been distributed to the members of the Committee a report from the Special Manager of the System Open Market Account on foreign exchange market conditions and on Open Market Account and Treasury operations in foreign currencies for the period July 18 through August 9, 1967, and a supplemental report for August 10 through 14, 1967. Copies of these reports have been placed in the files of the Committee.

In supplementation of the written reports, Mr. Coombs said that the Treasury gold stock would remain unchanged this week, but before the month was over the Treasury might have to show a reduction of at least $50 million. On the London gold market, intervention by the pool had cost an additional $37 million since the Committee's last meeting, necessitating the calling up of an additional contribution of $50 million from the pool members. The total contributed to the pool now stood at $470 million, as compared with an original figure of $270 million, with slightly less than $50 million on hand to finance further intervention. Demand on the London market had been somewhat easier during the past week or so, but the approach of the annual meetings of the International Monetary Fund and Bank

for Reconstruction and Development would probably stir up additional speculative buying and exert further pressure on pool resources.

On the foreign exchanges, Mr. Coombs remarked, the Belgian franc and Dutch guilder had remained strong and further use had to be made of the System's swap lines in both currencies. In the case of sterling, he had mentioned at the last meeting a number of ominous signs that a new crisis might be under way, and since then heavy drains on the Bank of England's reserves had developed. So far as he could tell, that did not reflect the reappearance of a large basic deficit in the British position. While the surplus earlier projected by British financial officials had pretty well withered away over the past few months, there was still reason to hope that they would end up the year in a roughly balanced position. The July trade figures just released this morning showed a strong recovery of exports and a dip in imports.

What had been doing the damage during recent weeks, Mr. Coombs continued, was a combination of factors. First of all, the United Kingdom tends to experience, just as the U.S. does, a heavy seasonal deficit in the third quarter of the year. That had been further aggravated this year by several unfortunate developments, such as the liquidation of Arab holdings of sterling and the German recession, which had had a temporarily depressing effect on British exports. Another trouble spot was the fact that the British money market no

longer enjoyed a competitive advantage in relation to the Euro-dollar market, with the result that earlier inflows of short-term funds into sterling were now tending to move back out. Furthermore, with no interest rate inducement to the market to shift Euro-dollar funds into sterling, the Bank of England was finding it increasingly difficult to roll over maturing forward contracts by executing market swaps; that is, buying dollars spot and selling them forward. Since the existing volume of forward contracts--and this was a highly confidential fact--ran into several billion of dollars equivalent, even a temporary failure to roll over maturing contracts could quickly mean a very sizable reserve loss; and that was what had been happening. Finally, and most important of all, there had occurred during the last few weeks a sharp break of confidence in sterling, with all the usual speculative consequences in such forms as an adverse shift of the leads and lags. That break of confidence was attributable in part to market recognition of the various difficulties he had just mentioned. Perhaps more importantly, however, it was attributable to a general feeling that the British Government had pretty well shot its bolt so far as major policy measures were concerned, that political loyalties within the Labor Party had been strained to the limit by the austerity measures already introduced, and that the program had failed to bring about a convincing recovery of sterling. The erosion of market confidence in sterling had been

further aggravated by a series of articles appearing in influential British publications, including The Economist, which had openly advocated devaluation as the missing ingredient in the Labor Government's program. Perhaps the July trade figures might bring some strengthening of confidence.

Mr. Coombs reported that during May, June, and July the Bank of England suffered losses of $800 million, of which $140 million was acknowledged as a reserve loss while the remaining $660 million was covered by recourse to central bank credit. Of the latter total, $450 million had been provided by the Federal Reserve and $210 by other sources.

Mr. Coombs said that so far in August, the British were again in the red to the extent of nearly $600 million, with some possibility that the deficit might approach or go over the $1 billion mark by month-end. In view of the relatively heavy use of the Federal Reserve swap line so far, he had been urging the Bank of England to make the fullest possible use of other credit facilities available to them. In July, the British drew $125 million on the so-called sterling balance credit package, and he would hope that they might be able to draw at least the same amount again this month. At the end of July, the U.S. Treasury provided $40 million in an overnight credit, and he would hope that they would be willing to put up considerably more, if necessary, during August. Nevertheless,

it was possible that the Bank of England would have to make further heavy drawings on the Federal Reserve swap line before the month was out. And in September a new speculative factor, namely, the approach of the Fund and Bank meetings, might intensify pressure on sterling still further.

Mr. Coombs thought it was possible, therefore, that the situation might be approaching a fairly dangerous point--perhaps more dangerous in certain respects than the speculative attacks on sterling in each of the three previous years. So far as British use of the swap line was concerned, unless otherwise instructed by the Committee he would propose to honor whatever requests for drawings they might make until the entire $1,350 million was exhausted. He would hope, however, that it would be possible to persuade the British to draw concurrently on other lines of credit totaling roughly $1 billion so as to lessen the burden falling on the System. Last year, the maximum use of central bank credit by the British reached a peak of $1.5 billion in September, and it was quite conceivable that this year their recourse to central bank credit might exceed last year's figure. That would be a very heavy commitment, particularly so in relation to their official reserves of slightly less than $3 billion. On the other hand, as he mentioned before, it would seem that most of the pressure hitting the British this year was of a speculative and seasonal nature. That was precisely

the situation for which central bank credit facilities had been designed, and he thought it would be a fatal blow, not only to central bank cooperation but to international financial cooperation more generally, if a speculative attack were allowed to overwhelm sterling or any other major currency which was not clearly overvalued.

Nevertheless, Mr. Coombs said, the very magnitude of the prospective British use of central bank credit facilities did raise an urgent question of whether they were doing everything possible to protect themselves. At the last meeting of the Committee he suggested that the Bank of England might usefully try to introduce a bit more flexibility in their discount rate policy in order to defend themselves against the competitive pull of the Euro-dollar market. The difficulty was that their interest rate system was so closely geared to changes in Bank Rate that it might be virtually impossible to move up British short-term rates appreciably above their current levels without an increase of, say, 1/2 per cent in Bank Rate. That would obviously present some political difficulties; and it might even be argued that such a Bank Rate increase might have a perverse effect by suggesting to the market that sterling had come under heavy pressure once more. He had made some discreet inquiries over the telephone to the Bank of England regarding the possibility of Bank Rate or other action, and had gotten the definite

impression that nothing was in the works. He had also had a number of conversations with U.S. Treasury officials as to other types of action which might be suggested to the British, and here again he had drawn a complete blank. He would hope, however, that that subject could be pursued in further meetings between Treasury and System representatives.

Beyond the immediate question of doing something to slow down the present rate of reserve loss by the British, Mr. Coombs commented, there was looming up a further serious question of what might be done to trigger a reversal of speculation against sterling, such as had been accomplished in 1965 and in 1966, through new credit packages reinforced by market operations. On this occasion, he would be very doubtful that it would be either desirable or possible to increase the very sizable credit facilities already available to the Bank of England, and he would doubt that market operations alone would suffice to bring about a shift in expectations. Consequently, there was a major risk that the debt now being built up by the Bank of England might prove difficult to reverse in any significant degree until early next year, when favorable seasonal forces reemerged. Meanwhile, of course, sterling would remain acutely vulnerable to any new setback with relatively little hope of raising new money to finance further reserve losses. He thought some serious conversations were needed with both the U.S. Treasury and the British on that matter to see if some new ideas would emerge.

Finally, Mr. Coombs suggested that the Committee should do some planning, again in consultation with the U.S. Treasury, for the contingency that the British might eventually be forced to devalue or to impose trade or exchange controls, or both, after having gone heavily into debt to the System and to other central banks. In such circumstances, he thought the British would be well advised to write off immediately their past losses by repaying at once all central bank debt through drafts upon their reserves. The central bank credit lines might then be fully reconstituted and would serve to cushion the transition to whatever new situation emerged. The alternative course of delaying repayment of central bank debts until the maturity dates, whatever they might be, would involve a major risk that the reflux of funds to London after a moderate devaluation or imposition of controls might not move fast enough or in big enough volume to permit repayment of central bank debt without having to show repeated reserve losses. Such a situation could easily lead--particularly if there had been a change in the British Government--to requests for prolongation or funding of the central bank debts, which would have repercussions on the swap network extending far beyond sterling. In any event, whatever might be the Committee's conclusions as to the most appropriate contingency planning, he thought the System would be well advised to make an approach to those problems, probably including informal conversations

both with the U.S. Treasury and with the Bank of England, well before the swap line was exhausted.

Mr. Mitchell remarked that he assumed Mr. Coombs was suggesting, in his concluding comments, that the risk to the System involved in British drawings on the swap line was a risk of illiquidity at a time when the United States could ill afford it rather than a risk of loss.

In reply, Mr. Coombs said he had been attempting to describe the situation that might face the Committee if the worst happened and sterling was devalued. If there was also a change in the British Government, the new Government might request repeated postponements of debts to the System that had been incurred under the present Government, and it might suggest that those debts be funded in one way or another. In his judgment, drawings on the swap lines were banking debts that should be honored on their due dates.

In reply to another question by Mr. Mitchell, Mr. Coombs said that any extensions of drawings under the existing swap arrangements were matters for negotiation between the parties and could not be made unilaterally. Of course, drawings did not have to be repaid before their maturity dates.

Mr. Scanlon asked how Mr. Coombs would assess the outlook for the London gold pool.

Mr. Coombs replied that he thought a crisis could easily erupt in the market for gold as well as in the market for sterling, and that if either occurred it would set off the other and lead to a general financial crisis. There had been some easing of pressures in the gold market in recent weeks; buying had been so heavy in July that demands were temporarily saturated. However, he would expect strong demands to reemerge by September at the latest. The situation in the gold market was similar in some respects to that in the market for silver, and the outlook was not good.

Mr. Maisel asked whether there was any possibility that the general structure of exchange rates might be considered in connection with any contingency planning.

Mr. Coombs commented that one of the most difficult aspects of contingency planning involving foreign participation was that it could easily precipitate the very contingency one was trying to avoid. He thought officials in all of the major industrial countries had some rough notion of how much of a break in any major currency could be sustained without precipitating a general break. He, for one, was not persuaded that sterling was overvalued, and he thought the British trade figures for July released this morning were suggestive in that connection.

Mr. Brimmer said he was troubled by Mr. Coombs' suggestion that if sterling were devalued the System should ask for repayment of British drawings not at their maturity but immediately, at a time when the British probably would need all the help they could get.

Mr. Coombs noted that he had not suggested that the System insist on immediate repayment of drawings if sterling were devalued. Rather, he thought it would be in Britain's own interest for them to acknowledge the full amount of their debts and to clear the books at the moment of any devaluation, rather than having information on outstanding debts emerge later, while they were struggling to recover.

Mr. Daane asked Mr. Coombs to amplify his remark that it probably would not be desirable to increase the credit facilities available to Britain in dealing with the pressures on sterling that might emerge in September.

In reply, Mr. Coombs observed that the situation this September was likely to be quite different from that a year earlier. The favorable market reaction to the announcement of a large increase in the swap lines in September 1966 was due in large part to the fact that it was possible to announce simultaneously that a full $1 billion of the enlarged System line with the Bank of England was unused. If a further increase in the size of the British swap line

was to be announced this year, it probably would come at a time when all or a major part of the existing $1,350 million line was in use. Under such circumstances a favorable psychological reaction was not likely. Secondly, any further substantial increase probably would make the swap line too large in relation to present British reserves.

Mr. Daane then asked about the possibility of enlarging the swap line before any new speculative attack on sterling occurred, on the basis of the recent strength in the British trade position.

Mr. Coombs replied that much would depend on developments in sterling over the rest of August. If the British had to make substantial further drawings on their line with the System--say, in the $400-$500 million range--they would not be left with much of a margin of safety. Under such circumstances, an increase in the size of the facility probably would be greeted with a hostile reception by other members of the swap network, on the grounds that the Federal Reserve was financing credits to the British by drawing on its other lines.

In response to a question by Mr. Bopp, Mr. Coombs said he had been told by a French official that in the event the British devalued the French would immediately follow. However, he was not fully convinced that would be the case; the fusion of farm prices among Common Market countries would make it difficult for any one

member to take independent action on its exchange rate. The key to the matter, he thought, would be the amount of any change in the British exchange rate. If the British were to devalue by 10 per cent, it was possible that other major countries would make no change; but the others were likely to react to, say, a 25 per cent devaluation by the British. At the same time, it was conceivable that a 10 per cent devaluation by the British might cause further speculation, if the market concluded that it was not large enough. In any case, he would emphasize that he did not think devaluation was either imminent or necessary. A stormy season lay ahead for sterling, however, and his purpose was to bring some possible risks to the attention of the Committee.

Mr. Galusha asked whether his understanding was correct that Mr. Coombs thought the measures the British were taking, in themselves, should prove sufficient to right the matter.

Mr. Coombs replied that that was his view. The difficulty was that the British had experienced one bad break after another. Moreover, the Government was faced with a hostile press, and with large elements within and outside the Labor Party that objected to the measures taken.

Mr. Daane commented that when the Chairman and he were in London a few weeks ago Chancellor Callaghan had both publicly and privately made clear his own view that devaluation of sterling would

be of no use, and that the measures the British had taken would have proved effective by now had it not been for the Mid-East hostilities and other unexpected developments. He (Mr. Daane) personally was convinced that the Chancellor was sincere in those views. There were, of course, other voices in the Government and he did not know whether the Chancellor's would continue to prevail, but Mr. Callaghan appeared determined to try to maintain the present exchange rate for sterling.

Mr. Brimmer referred to Mr. Coombs' comment about the possible desirability of a change in Bank Rate, and asked whether an alternative might be found in operations undertaken to narrow the forward rate spread.

Mr. Coombs replied that the forward rate spread was already fairly narrow. The British had a hugh volume of forward contracts outstanding and might be able to do a little more in that area, but it was not likely to be easy.

Mr. Hickman noted that short positions in sterling were fairly large at present. If the new trade figures led to any temporary improvement in the pound he presumed the Account Management would consider the possibility of buying in the market in an effort to put a squeeze on those in bear positions.

Mr. Coombs noted that such an operation had been carried out with considerable success in September 1965, but a similar

operation attempted in July 1966 had run into strong resistance. Such an operation might be useful at some point in September. One difficulty, however, was that much of the ammunition that would be needed for it had already been used.

Mr. Robertson agreed that there was a need for contingency planning. He noted that conversations between the System and the Treasury on that subject had been launched, and that the groundwork for discussions between the Treasury and British officials had been laid.

> By unanimous vote, the System open market transactions in foreign currencies during the period July 18 through August 14, 1967, were approved, ratified, and confirmed.

Mr. Coombs then noted that four System drawings on swap arrangements, all in Swiss francs, would reach the end of their three-month terms soon. These consisted of two drawings on the Swiss National Bank, in the amounts of $47 million, maturing August 31, 1967, and $100 million, maturing September 8; and two drawings on the Bank for International Settlements, in the amounts of $85 million, maturing August 31, and $100 million, maturing September 7. He thought it probably would prove desirable to renew those drawings for further periods of three months since a major turn in the Swiss franc situation did not appear imminent.

Renewal of the four drawings was noted without objection.

Before this meeting there had been distributed to the members of the Committee a report from the Manager of the System Open Market Account covering domestic open market operations for the period July 18 through August 9, 1967, and a supplemental report for August 10 through 14, 1967. Copies of both reports have been placed in the files of the Committee.

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

> Treasury financing and the President's tax proposals have held center stage in the financial markets since the Committee last met, and will continue to do so in the period immediately ahead. Hearings started yesterday in the House on the tax bill and the Treasury will be announcing a cash financing later this week.
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> In its August refunding, the Treasury offered on July 26 for cash a 5-1/4 per cent, 15-month note priced to yield 5.30 per cent. Just preceding the offering yields in the intermediate area had risen rather sharply, and there were wild fluctuations in bidding ideas in the one-year bill auction held on July 25. The actual average issuing rate in that auction turned out to be 5.15 per cent, as much as 1/4 per cent below some bidding ideas earlier that day. Investment demand for bills at the higher yields, and dealer short covering in the intermediate area created a better market tone by the time the Treasury announcement was made and facilitated pricing of the new issue. While the market viewed the new issue as attractively priced, there was some disappointment that a longer option was not included in the refunding. Dealers have reported good progress in working down their allotments of about $1/2 billion of the new notes, which will be issued and paid for today, although many sales had to be made below the issue price. It was only last night that the new note was back to the issue price of about 99-30/32.

The President's tax message, long awaited by the market, led to a momentary price rise of Government securities. While the proposals were even stronger than the market had anticipated, the initial optimistic market response was extremely short-lived because of the indicated size of the deficit even after taking account of the new taxes, uncertainties about Congressional response to the proposals, and the knowledge that Treasury financing needs over the rest of the year would not be greatly reduced even if the tax proposals were passed. Strong professional selling pressure then pushed prices of Treasury notes and bonds lower, until near the close of the period. It can only be hoped that as testimony on the tax bill proceeds, the results of the mid-year budget review are made public, and the Treasury's August cash financing is disposed of, the market will be able to assess the tax proposals more dispassionately. While uncertainty will persist until final Congressional action is taken, the President's tax proposals would obviously be extremely helpful in bringing about a greater measure of balance in financial markets as well as in the economy generally.

As noted, interest rates on Government obligations fluctuated rather widely over the period, despite a stable Federal funds rate and ample reserve availability. On balance, yields on coupon issues rose by 10-20 basis points over the period. The three-month Treasury bill rate was little changed, but rates on longer bills rose by 10-30 basis points. In yesterday's bill auction, the average rates on three- and six-month bills were established at 4.19 and 4.79 per cent, respectively, about 5 basis points below and 5 basis points above averages set in the auction just preceding the last Committee meeting.

The corporate and municipal markets fared somewhat better than the Government market. In the municipal market rates moved lower during most of the interval, as the calendar was relatively light and the attractiveness of such bonds was enhanced by the prospects of a tax increase. Demand for tax exempts tapered off toward the end of the period, however, and rates edged up from earlier lows. Rates on new corporate issues inched higher but investment demand remained strong at current yield levels. Although the calendar is currently running somewhat below recent levels, it is apparent that a number of large new issues are under active consideration.

There was little need for open market operations to affect reserves over the period since the Committee last met. The net supply of reserves over the period amounted to only about $50 million, reflected in a rise in the Account's holdings of Treasury bills. There were no transactions in coupon issues, except for the exchange of $5.9 billion of maturing August 15 issues for the new note in the Treasury's refunding. In fact, the System was in the market on an outright basis on only one day--July 24--with repurchase agreements being made on August 3 and August 10. Free reserves fluctuated rather widely from week to week, reflecting shifts in country bank excess reserve levels, but the Federal funds rate was generally steady--averaging a bit under 4 per cent.

Aggregate reserve and credit measures expanded sharply in July, as the blue book[1/] notes, and average projections for August are also on the high side. The current July-August projection of the bank credit proxy is for an average growth rate of 14-16 per cent, as compared with the 10-12 per cent growth rate projected at the time of the last meeting. As the blue book explains, part of this discrepancy is due to changed assumptions about the Treasury financing pattern. However, in the absence of even keel considerations, I would have interpreted these aggregate measures--in light of the proviso clause--as calling for some modest firming of money market conditions. In practical terms this would probably have meant that we would not have made RP's on August 10, and possibly not on August 3 as well, and would have let the Federal funds rate run above the discount rate for a period of several days. In the event, however, considerations involving the Treasury refunding, in my judgment, were such as to dominate the proviso clause. While distribution of the new Treasury issue was proceeding reasonably well, the note was below issue price bid. Moreover, the market has not yet regained a sense of balance or confidence so that it can withstand even a moderate firming of monetary policy without a substantial interest rate reaction.

Looking ahead, the System will, on current estimates, have to provide a substantial volume of reserves over the

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1/ The report, "Money Market and Reserve Relationships," prepared for the Committee by the Board's staff.

next four weeks--about $600 million on Board staff estimates and even more on New York Bank staff estimates. The international uncertainties which Mr. Coombs has noted may mean, however, that a substantial portion of these reserves may be supplied by foreign currency operations rather than by domestic open market operations. Even keel considerations, in my view, will probably preclude any substantial operations in coupon issues, but do not rule them out entirely. I should note that there is a major discrepancy--at least at the moment--in the projections of the September bank credit proxy between the Board staff and New York, with our projections indicating a growth rate about double the 7 - 9 per cent range contained in the blue book. Even keel considerations are, in any event, likely to dominate the proviso clause again, but as always, it will be helpful if individual Committee members will comment on their interpretation of the language suggested by the staff.

The Treasury is planning to announce, probably on Thursday, the terms of its cash financing which is expected to raise about $2-1/2 billion. The books would be open on Tuesday, August 22, with payment scheduled for August 30. A note offering is expected but the maturity has not yet been decided on and obviously will not be until the last minute. There is a strong school of thought in the market that favors the issuance of a note maturing close to seven years, that would require a 5-1/2 per cent coupon. Such an offering would appeal to a broader group of investors than a shorter dated issue bearing a lower coupon, and some believe it could act as a catalyst on the market. There is a risk that a 5-1/2 per cent coupon would bring about greater competition with savings flows into thrift institutions and with private credit markets generally. But a shorter-dated issue that met only a mediocre reception might cause more pressure on shorter rates and lead to even greater problems for the thrift institutions. I suspect that a 5-1/2 per cent coupon does not have the same magic today as a five per cent coupon had in 1960, and that, while risks are involved, they are not major ones. The Treasury needs a successful financing now, with some debt extension, in order to help restore market confidence. Once this cash financing is completed, the Treasury should be out of the market until it has to begin to meet major cash needs in early October--presumably through tax bills--although there could be an intervening PC issue by the Federal National Mortgage Association.

Mr. Mitchell referred to Mr. Holmes' comment that in the latter's judgment considerations involving the Treasury refunding had dominated the proviso clause in the recent period. He asked how long Mr. Holmes thought the Treasury's expected cash financing might dominate a proviso clause if one were included in the directive to be issued today.

Mr. Holmes replied that it was hard to say, since the answer would depend on the nature of the offering, how it was received, and how rapidly distribution was carried out. With $2-1/2 billion in notes to be issued, even keel considerations certainly would hold through payment date and, he suspected, somewhat longer.

Mr. Maisel asked how the Manager would interpret the proviso clause included in the draft directive submitted by the staff,[1/] particularly in light of the large difference between the New York Bank and the Board staffs' projections of the bank credit proxy.

Mr. Holmes replied that he would hope to get help from the Committee on that question. However, assuming the term "current expectations" in the draft directive was taken to mean the projections given in the blue book, any apparently significant deviation of bank credit growth below a 7 per cent rate would lead him to permit money market conditions to ease a bit. In that

1/ Appended to this memorandum as Attachment A.

connection, a question arose as to whether the Committee would want the Desk to offset any easing of conditions that resulted from an auto strike. If, on the other hand, bank credit expansion appeared to be deviating significantly above a 9 per cent rate, he would let conditions tighten to some extent. As he had noted, however, even keel considerations might prove extremely important, and in his own view such considerations should come first. The situation was certainly complicated by the fact that the projection of the New York Bank staff was much higher than that given in the blue book, and he found it hard to judge which of the two projections was better.

> By unanimous vote, the open market transactions in Government securities, agency obligations, and bankers' acceptances during the period July 18 through August 14, 1967, were approved, ratified, and confirmed.

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

Mr. Brill presented the following statement on economic conditions:

The latest green book[1/] is pleasant reading indeed, especially for one who has been away from the domestic scene for a month or so. The evidence is persuasive that the economy is shaking off the forces that retarded expansion earlier, and there are many portents of further acceleration in activity. Most of the evidence has been detailed in the green book and in last Friday's supplement--rising retail sales, rising new orders, higher employment, a better inventory position, and the beginning of a pick-up in industrial production. It now looks as though we were conservative in our first rough estimate of the production pick-up, for the manhours data subsequently available put the July increase at a full point in the index, rather than the half-point estimated earlier.

Before plunging into a consideration of the problems that renewed prosperity will bring, it may not be inappropriate or immodest to note the achievements of what some editorialists disparagingly refer to as the "new economics." Prompt and appropriate monetary and fiscal stimuli have succeeded in carrying the economy through a period of marked reduction in consumer spending propensity and massive business inventory adjustment--so massive as to dwarf inventory shifts in earlier postwar cycles--all in record time, with minimal impact on unemployment and with significant slowing in the rise in prices.

But the speed of the adjustment itself has created some problems, and the "new economics" cannot be crowned with success until it demonstrates the capacity to live with, as well as to achieve, relatively full resource use. The immediate problem revolves around future price developments. There is mounting evidence that industrial commodity prices are beginning to stir, after stability this spring and early summer, and, indeed, after a rise of less than 1 per cent from mid-1966 to mid-1967. Recently, some industrial materials prices have strengthened, and a spate of increases have been announced for finished products.

1/ The report, "Current Economic and Financial Conditions," prepared for the Committee by the Board's staff.

Testing of markets was bound to occur as economic activity picked up. The critical question is whether such price increases are likely to spread, and possibly to accelerate. Unfortunately, I think the most likely answer is yes, at least in the short run. A situation of renewed economic growth, rising incomes, and more buoyant markets--following a period of narrowing profit margins and with rising wage costs in prospect--seems to me highly conducive to price boosts.

One can muster arguments to the contrary, of course. Despite the narrowing in profit margins--in manufacturing, the profits-to-sales ratio has fallen from 9.8 per cent in early 1966 to 9.0 per cent at the end of the year and to a little over 8 per cent in the second quarter of this year--the decline leaves margins not far from the average over the past decade, and well above recession lows in earlier cycles. The profits pinch is real, but it isn't as bad as has been made out.

Further, it can be argued that when 15 per cent of manufacturing capacity is idle, and with slack foreign markets moderating materials demands and adding to potential product supply here, competitive forces will limit the scope for price advances. Finally, return to a faster rate of growth should produce substantial gains in productivity, particularly in light of the heritage of a three-year investment boom which is putting a large volume of efficient plant on stream.

But there are strong pressures countering these moderating forces. Wages are likely to continue to rise rapidly as higher contract settlements spread. Among manufacturing workers, particularly, there is undoubtedly going to be an intensive effort to make up for the decline in real wages over the past year, to undo some of the compression that has occurred in wage differentials among skills, and to match wage-rate gains that have occurred in a number of non-manufacturing industries. Increased productivity may offset some of the effects of rising wages, and thereby slow the rise in unit labor costs, but one has to be quite optimistic to anticipate any <u>decline</u> in costs. In fact, some rough guesses made in the framework of our current GNP projection have unit costs still rising at about a 3 per cent annual rate in the second half of the year--down sharply from the recent rate of advance, but still large enough to continue exerting pressure on profits.

Under these circumstances, the natural objective of managements to maintain profit margins, let alone to restore earlier higher margins, can be achieved only by raising prices. And they're not likely to wait until capacity utilization reaches 90 per cent to try, particularly if rising sales suggest that modest price hikes can be made to stick. After all, industrial prices began to rise in 1958, when production was at far lower rates of capacity utilization than currently. While several underlying factors suggest limits on the extent to which prices may advance, it's likely that we're at the end of the industrial price stability of recent months.

Unfortunately, I don't quite see the socially acceptable public policies that can prevent this in the very short run. The staff's projection indicates that even with enactment of the President's tax program on the time schedule and in the amounts proposed, aggregate demands would still be advancing rapidly this fall, rapidly enough to encourage producers to at least try to pass through further rises in costs before the full effect of the program dampens demands effectively. Nor--judging from what we have learned about lags--would an intensification of monetary restraint today likely have sufficient impact on real activity in the short run to restrain prices this fall. It might not take much more restraint to push interest rates to the point where thrift institution flows were threatened, particularly with another dividend crediting period coming in five or six weeks. But short of a financial squeeze of 1966 proportions, mortgage commitments and fund availability in hand would still likely carry housing activity forward over the balance of the year.

What this adds up to is an unhappy conclusion that the Government has probably lost a battle to prevent some price increase in the short run, and should concentrate its strategy now on winning the longer-run goal of preventing cumulation or even continuation of inflationary pressures into 1968. Here the outlook seems brighter. The fiscal program being pushed vigorously by the Administration is a strong one in its ultimate impact, and given the many signs of renewed expansion and rising price pressures--as well as the large deficit numbers being bandied about--I

find it hard to believe that the program will not be enacted in large degree. Perhaps the timing and amount will in the end not be all that one would desire, but substantial fiscal restraint in 1968 seems a fairly good bet.

Monetary policy also seems appropriately positioned for the longer run. The costs of financing expenditures on credit are already back to historically high levels, and Treasury financing needs, along with the queue of private borrowers waiting in the wings for a crack at the flow of funds, could keep market rates relatively high in coming months. Indeed, our present posture might well be made somewhat more flexible by a return to the two-way proviso, which would permit financial market pressures to ease if basic demands in the economy respond more promptly to prospects of fiscal restraint than has been projected by the staff, or if, as I would wager more likely, demand trends are obscured by a major strike beginning before the next meeting of this Committee.

Mr. Hickman remarked that he would like to understand a little better than he did the advantages Mr. Brill saw in the Committee's trying to offset the effects of an automobile strike by easing money market conditions. The advantages of having a slack money market during a strike were not clear to him.

Mr. Brill noted that an auto strike might tend to reduce bank credit growth to a rate below that projected in the blue book. If the directive included a two-way proviso, calling for modification of operations in the event of significant downward as well as upward deviations from the projection, the Desk would be able to permit whatever easing was concurrently taking place in money market conditions. He did not think that a two-way proviso would require

that aggressive operations be undertaken by the Desk in order to produce easing, under those circumstances.

Mr. Mitchell observed that both the System and the Administration were gearing up to act against the possibility of a renewal of inflationary pressures, and for some time the staff had been alerting the Committee to that problem. With all of the recent discussion about the need to resist inflationary pressures by use of either fiscal or monetary policy, he was somewhat surprised to hear Mr. Brill recommend a symmetrical proviso clause that would seem to imply that the pressures were equally likely to develop or not.

Mr. Brill replied that of the various possible causes of reduced demands the one he thought most likely at present was a strike in the auto industry. If such a strike resulted in a sharp reduction in output, he would not see much sense in monetary tightening of the sort that would result from an effort to maintain prevailing money market conditions.

Mr. Mitchell remarked that the strike expected was not a general one; it was likely to affect only one producer in the automobile industry, and according to some staff opinion it probably would last for only a limited length of time.

Mr. Brill commented that the best information at present was that a strike would begin in September and initially would

affect one producer, but he was not prepared to forecast the length of a strike. Although a work stoppage was not likely until late in the interval between Committee meetings, credit demands might be affected earlier by anticipations of a strike--say, by suppliers of auto parts.

Mr. Axilrod expressed the view that a symmetrical proviso clause did not necessarily imply that the two eventualities for which instructions were given were equally likely.

Mr. Brimmer noted that the Manager had asked for comments by Committee members on their interpretation of the language of the proviso clause in the draft directive. In that connection, some attempt to reconcile the divergent projections of the Board and New York Bank staffs would seem to be required. He wondered whether Messrs. Brill or Axilrod had any additional comments on how firmly the Board staff held to the projections given in the blue book.

Mr. Axilrod suggested that that question be deferred until after his remarks concerning financial developments. He then made the following statement:

> In financial markets we are in a period in which dominant credit market influences are Governmental credit demands and expectations of a tax increase based on the President's fiscal message, though the expectations cannot yet be described as very firmly held and their positive impact on markets is diluted by uncertainties with respect to timing and amount of any prospective increase. We have emerged from a

period, the first half of the year, in which credit market demands were wholly from private sectors of the economy and weighted strongly by business needs to pay accelerated taxes; and in which the monetary policy pursued was sufficiently easy to permit, among other things, the redirection of the supply of funds in financial markets to financial intermediaries, including banks. Because of the strong showing of intermediaries--which has continued thus far in the summer--the availability of mortgage funds has increased substantially and the flow of mortgage commitments and credit appears to have withstood fairly well the tightening of capital markets that has developed since last winter.

The most important factor easing the position of intermediaries was the continuation during most of the year of relatively low short- and intermediate-term interest rates. While monetary policies perhaps contributed most to those interest rate developments, they were also a result of the Federal Government's debt management policies. The Treasury's cash balance was not increased as it usually has been during the first half of the year, so that the Federal Government could make a substantial amount of new debt repayment chiefly in the bill area.

With a sizable cash deficit now in prospect and the cash balance already relatively low, the Federal Government will have little alternative in the current half year but to borrow substantial amounts. We now tentatively estimate borrowing in a $16 - $18 billion range, including some PC offerings, assuming passage of the tax increase as proposed but also assuming that non-defense outlays are not reduced to the full extent called for in the recent fiscal message. Borrowing of this amount is more than double the second half of last year and is roughly in line with our expectations at the time of the staff projections presented to you in June.

About $6 billion of this borrowing already has taken place or has been announced, and another $2 - $2.5 billion will probably be announced later this week, as Mr. Holmes has already noted. Treasury bill rates, other short-term rates, and yields on intermediate-term U.S. Government coupon issues have already risen markedly since late spring in response to these financing needs. These pressures may have been an additional factor

affecting long-term markets. But in the past few weeks municipal yields edged downwards, and an optimist might suspect that some of the pressures in corporate bond markets may ease off as the recent very heavy calendar moderates. However, there are enough hints in the wind that corporate demands may yet again be larger than suspected and may help generate enough over-all capital market pressures to suggest that System purchases of coupon issues could continue to be a useful adjunct to over-all operations.

While the rise in short- and intermediate-term rates has not reached the point where it has triggered movements of funds away from financial institutions, the rise has been limited only by a rapid recent expansion in bank reserves. It should be stressed, though, that this expansion was influenced not only by Governmental demands but also by large business loan demands in June and early July. Just as last year, there was a marked acceleration in corporate tax payments that affected loan demands in the first seven months of the year, with our seasonal adjustments lagging events, and it may just be that business loan demands will be more moderate in the coming months.

A more moderate expansion of business loans in the future would enable the additional Treasury cash borrowing to be financed without any acceleration of bank reserves and other aggregate monetary variables from recent rates, and probably with a lessened pace of expansion. The public debt is not likely to be all placed with banks, and clearly the new tax bills which are likely to be the main instrument used for the fourth-quarter cash needs will not remain for long in bank hands. Some of the public funds going into Treasury securities may represent a displacement of funds from financial intermediaries, but under current monetary conditions, such displacements are likely to remain quite moderate--and within limits not necessarily detrimental, since intermediaries, including banks, are in a substantially improved liquidity position and the economic outlook is turning more bullish.

The interest rate margin left before disintermediation would become a major problem--given the present ceiling rates on time and savings deposits

and on savings shares--may be around 75 basis points in the short bill area, taking the 3-month bill rate as a touchstone, and less in longer bills. So long as the Federal funds rate remains around the discount rate and both remain around 4 per cent, it is difficult to foresee circumstances--barring jarring international news--which would cause short bill rates to rise by that much. However, it would probably take a more moderate rise in intermediate coupon and Federal agency issue rates from current levels to cause some disintermediation, which might begin to appear if Treasury intermediate coupon issues rose to 5-1/2 per cent or better and Federal agency issues to 6 per cent. We are within 25 to 50 basis points of such yields, and if a tax increase appeared unlikely or it was thought that monetary policy might be tightening, expectational forces would help drive yields up to such levels rather quickly.

Putting all these strands together, and given the economic outlook, suggests to me that the Committee should stand pat at this meeting, particularly in view of the Treasury financing and the proposed fiscal program. It does seem desirable, however, to replace the current one-way proviso with one that is two-way. On principle, that would generally seem to be the best sort of proviso, since the main purpose should be to provide a safeguard against either a significantly larger or significantly smaller expansion in credit demands than the Committee considers it desirable to tolerate under the existing interest rate structure.

Also, at this time, all the well known uncertainties surrounding the fiscal program, and others surrounding the possibility, duration, and effects of an auto strike, suggest a flexibility in operations that might be signaled by a two-way proviso. But the difficulties these imply for projections, together with even keel considerations, also suggest that it might require rather substantial departures from expectations to trigger the proviso. For example, one might suggest that the proviso would be triggered if bank credit were to begin moving so that the September average looked as if it would be plus or minus maybe as much as 5 percentage points either side of the current 7 - 9 per cent projection. In view of the recent sharp growth in bank credit in July and early August, one might argue that the Committee should be more concerned with too large

> a bank credit increase rather than one that was smaller than projected. But should reserve growth fall off sharply, it may be desirable to permit some slight easing of money market conditions so as to avoid appearing to restrain money and credit growth sharply at a time when a program of fiscal restraint was in the wings.

Turning to the question Mr. Brimmer had raised earlier, Mr. Axilrod noted that the Board and New York Bank staffs' projections both employed the same assumptions regarding Treasury financing operations. He strongly suspected that the difference in the projections was attributable mainly to divergent expectations for business loan demands. The Board's staff did not expect demands to be particularly strong in August and September, although perhaps picking up in September. In that connection, he noted that repayments of bank loans had been large in early August. He personally did not expect the rate of growth in business loans during the next few months to be as large as in June and July.

Mr. Swan referred to the earlier discussion of the desirability of a two-way proviso clause and observed that there were two possible consequences of a strike that should be distinguished. One was some easing of money market rates, and he understood that Mr. Brill thought it would be undesirable to offset such easing. The other was slower growth in bank credit. If a strike produced the latter result he could see no reason for attempting to restore the growth rate. Of course, there might be both an easing of rates and a slowing of bank credit growth, in

which case no offsetting action would seem to be required. It was not clear to him, however, which of the two possibilities the staff had in mind in suggesting a symmetrical proviso clause.

Mr. Brill commented that he had been thinking about the easing of money market rates as a result of increased availability of funds from any companies that were struck. Early in the strike period those companies would continue to receive revenues but their payments would be sharply reduced. Presumably they would invest their added funds in short-term market instruments, and that would affect the pattern of short-term rates.

Mr. Axilrod added that, as he understood it, the proviso clause did not introduce bank credit as a specific target; it did not call for operations to maintain bank credit growth at any particular rate. Rather, the proviso called for a change in money market conditions if bank credit moved in a specified way. Thus, if a two-way proviso clause was used and the strike led to slower bank credit growth, the Desk presumably would make less effort to offset any concurrent easing of money market conditions.

Mr. Brimmer asked whether the staff expected U.S. bank borrowings through foreign branches to continue to add about 1 or 2 percentage points to the growth rate of bank credit as reflected by the proxy.

Mr. Axilrod replied that the borrowings in question had been running at about that rate in the last month or so, but

specific projections had not been made for them. In his view, such borrowings tended to fluctuate with changes in the volume of CD's outstanding.

Mr. Daane noted that Mr. Axilrod had expressed the view that System purchases of coupon issues might continue to be useful. He (Mr. Daane) had not been present at the preceding meeting of the Committee, but he gathered from reading the memorandum of discussion for that meeting that the subject had been actively considered. In particular, he noted that Mr. Robertson had suggested that coupon operations be undertaken only under relatively limited conditions. He asked whether Mr. Holmes would indicate how he understood the Committee's views with respect to coupon operations.

Mr. Holmes commented that he interpreted the Committee's posture on the matter to be much the same as it had been earlier in the spring and summer. For the period immediately ahead the Treasury financing imposed some restraint on coupon operations, but he did not think that they should be ruled out entirely if proper conditions existed. He would summarize those conditions as involving a need to supply reserves, availability of coupon issues in the market, and the absence of any fundamental readjustment under way in the market at the time.

Mr. Reynolds presented the following statement on the balance of payments and related matters:

When Mr. Brill described the green book as pleasant reading, he was, of course, referring only to three-quarters of it--that portion that deals with domestic developments. The balance of payments news is not reassuring. The foreign trade balance did not improve further in May and June; the liquidity deficit remained large in July, though perhaps not so large as during the first half year; and while the official settlements deficit swung temporarily into surplus as a result of large inflows from the Euro-dollar market, this appears to have been partly at the expense of sterling--as in past summers--and does not represent a sustainable situation.

More generally, the year 1967 is proving to be a great disappointment to those who had hoped for some progress toward international payments adjustment. The U.S. deficit is running much larger this year than last. The United Kingdom is not achieving the basic payments surplus that it needs to pay off short-term debts, and has recently suffered from renewed capital flight. And continental Europe continues to run a very substantial surplus, although that surplus is now concentrated in Germany rather than in France and Italy.

One central reason for all these disappointments has been the depth and persistence of Germany's first major postwar recession, which has reduced employment there by about 3 per cent and industrial production by 10 per cent since early 1966. That recession has affected other continental European countries, and some of them--notably France--have also experienced some independent weakening of domestic demand. In turn, recession on the continent has damped the exports of this country and of Britain, and has tended to boost U.S. and U.K. imports, as the depressed industries of Europe have sought external markets more aggressively. Finally, the U.S. and the U.K. economies have themselves been sluggish, though much less so than the German, and thus have contributed to the pronounced leveling off in world trade and world economic activity that has characterized the year 1967 to date.

We need to judge how important these differential business cycle effects have been if we are to appraise the underlying trends and outlook for our own balance of payments and for Britain's. Accordingly I have attempted some very rough calculations, on the assumption--which may be optimistic--that the imports of Italy and Japan will continue to advance and that those of European countries other than Italy will be about as large in the second half year as they were in the first half.

On this basis it appears that German imports this year may be about $2-1/2 billion or 14 per cent below what might be termed their reasonably high-employment level. And the imports of other continental European countries may be about $3 billion or 7 per cent below their high-employment level, for a total shortfall of about $5 to $6 billion.

Meanwhile, continental European exports may be only $3 to $4 billion below a trend consistent with high employment everywhere, so that the trade balance of the continent may be about $2 billion above trend this year.

For the United States, on the other hand, I would judge that imports are not very far from their high-employment trend level. They have come down only moderately from a level that was clearly swollen by excessive domestic demand pressures, and are still unusually high in relation to domestic activity. Apparently the effects of the modest softening of domestic demand early this year are being felt only with a lag, and are being partly offset by the effect of recession in Europe in pushing exports this way. That, at least, is roughly the hypothesis that underlies our present projections.

U.S. exports, meanwhile, are being held down this year as slack European demand makes itself felt both directly and via the reduced earnings in Europe of third countries and the more intense competition of European goods in those countries. One may guess that U.S. exports and the trade balance are running $1 billion or more below trend this year.

On similar reasoning, the U.K. trade surplus has also been depressed this year--probably by at least $1/2 billion--by the differential impact of business cycle developments.

From these rough attempts at quantification, which I am so far unable to carry beyond the merchandise trade sector, it seems clear that the United States would still have a substantial--though smaller--deficit even in a full employment world, at least so long as Vietnam costs follow their recent path. Hence, I am persuaded that we urgently need both general economic restraint--the tax increase--and probably also some additional specific restraint, perhaps on direct investment outflows, if the payments situation is to remain manageable in 1968. In this situation, monetary policy should probably also tilt

toward restraint to whatever extent it can do so consistent with reasonably high domestic employment.

For the United Kingdom, this year's cyclical balance of payments shortfall of $1/2 billion or more is crucially important. It represents roughly the margin between what Britain hoped to achieve this year on the basic balance and what it is actually achieving. The sort of calculation that I have attempted must be figuring importantly in current British assessments of the viability of the present exchange rate, since it is the disappointing trade balance much more than any other single factor that is causing renewed uncertainty about sterling. The July trade improvement, announced today, is helpful, but it does not suffice to remove all doubts.

Much depends on how soon a cyclical recovery in Europe--especially in Germany--may be hoped for. Early this year, the prevailing forecast was for a German upturn just after mid-year. More recently, most analysts have tended to put the upturn much later, perhaps not until 1968. But the Bundesbank in its latest Monthly Report already sees some signs of recovery--notably in the inventory situation; in new orders for steel products, partly as a result of the Government's first supplementary investment program; in imports, which turned up in June; and in the German stock market, which has moved up more sharply than at any time since 1960.

So far, these are only a few straws in the wind. But at least it seems possible that our balance of payments and Britain's will get a little, much needed, support from an improving business situation on the continent later in the year. Even with such a turn, however, the period ahead will be a very difficult one from the payments point of view.

Mr. Robertson then called for the go-around of comments and views on economic conditions and monetary policy, beginning with Mr. Treiber, who made the following statement:

The most important development since the last meeting of the Committee is the President's message of August 3 to the Congress recommending a comprehensive program to reduce the nation's budgetary deficit; the key recommendation is, of course, the temporary

surcharge of 10 per cent on individual and corporate income taxes. Prompt and decisive fiscal action by the Congress would go far to help assure that the renewed growth in the economy is held to a sustainable pace with a reduction in pressure on prices and in the tensions in the money and capital markets. It would, of course, lessen the need for monetary policy to carry an excessive share of the over-all anti-inflationary effort, as was the case in 1966.

As the President reported, Federal Government expenditures, particularly for defense, have continued to rise at a fast rate--much faster than indicated in the January budget estimates. At the same time private spending is once more rising across a broad range. The outlook is for strong advances in economic activity.

Employment has risen further and the over-all unemployment rate has dropped slightly. For more than a year and a half, it has been at or below the 4 per cent interim full employment goal suggested by the Council of Economic Advisers in 1961.

The rise in consumer prices has been accelerating, although so far the acceleration has been confined to the food area. Many wage settlements this year have provided increases much greater than the increases in general productivity, and wage demands in current bargaining sessions are large. Thus, pressures of increased demand on an economy with little slack, coupled with upward cost pressures, threaten an even more rapid increase in prices.

Deposit and share accounts at thrift institutions have been rising rapidly. Bank credit continues to grow at a rapid rate, and a large increase is forecast for August. Corporate and municipal borrowing in the capital markets has been very high. Yields on some types of long-term obligations have exceeded last summer's peaks. The prospect of large U.S. Treasury borrowing in the second half of 1967 and a growing belief that the rate of economic advance will accelerate sharply have weighed more and more heavily on the markets. They continue to be heavy even after the President's message.

Our adverse international balance of payments is a cause of great concern. The liquidity deficit for the second quarter and for the entire first half of 1967 was a good deal higher than that experienced in 1966 despite the enormous lift this year from special transactions.

Several countries of continental Europe added substantially to their dollar holdings and we have had to make greater use of our swap facilities. Still further use appears in prospect.

Our trade surplus is larger than in 1966, but it is far below the level of 1964. A marked increase in our exports is unlikely in the light of conditions in some of the major European markets to which we customarily export; and inflation at home would, no doubt, raise our imports. Inflation would weaken the position of the dollar internationally at the very time our worldwide efforts require that confidence be sustained and strengthened.

Outflows of capital, especially direct investments, are large and probably will continue to be large. It seems to me that the voluntary program to limit direct investment abroad, being administered by the Department of Commerce, should be tightened substantially and promptly.

These developments at home and abroad make imperative prompt action to slow the growth of over-all demand in the American economy. Prompt fiscal action is called for, and this is what the President has recommended. We have before us the question whether monetary restraint is also called for. I think that today the answer to the question is "no." It is too early to have an opinion as to whether there may be an undue delay in obtaining fiscal legislation and the Treasury is about to announce its plans for a public offering of a new issue of securities for cash. These two factors counsel no change in credit policy today.

The directive drafted by the staff appears generally appropriate for the present situation. But it does seem to me that it would be desirable to emphasize our concern about the balance of payments problem. I suggest therefore that the sentence stating that "the balance of payments deficit has remained substantial" be expanded by adding the words "and is a serious national problem." Since most of the period ahead will be dominated by even keel considerations, I doubt that the two-way proviso clause will come into play.

Mr. Ellis reported that most of the recent economic indicators of New England business had registered small

changes--sometimes offsetting--that built up to a posture of strength but not expansion. Surveys of expected activities generally supported the national projections of renewed expansion making a gradual impact.

Perhaps the current situation in the New England shoe industry would illustrate both opportunities and problems that faced others, Mr. Ellis said. New England shoe producers, who accounted for about one-third of the national output, had had a disappointing first quarter but their sales had picked up after Easter and by now year-to-date sales were a little above year-earlier levels. Production, however, had slipped to a 9 per cent shortfall and manufacturers now felt it unlikely they would achieve the production figure of 655 million pairs--a 2 per cent increase--they had projected for the year. The shoe manufacturers listed two problems. Of first importance was the "rising flood of imports." During the first five months of 1967 imports rose 33 per cent over the same period last year, and the industry feared imports might amount to 20 per cent of domestic production for the year. Senators Muskie and Margaret Chase Smith of Maine had each introduced bills to provide for the imposition of a quota system. The second problem, significant since the industry had not been attempting to expand, was a continued shortage of skilled and unskilled labor in certain shoe centers and key operations.

Turning to monetary policy, Mr. Ellis commented that since the Committee's last meeting new evidence had become available on the two major uncertainties facing the Committee. Evidence on the gathering strength of the economy, as reflected in new orders, manufacturing output, employment, and so forth, pointed to expansion as the likely immediate course of the economy. The President's tax message reduced, although perhaps only slightly, the uncertainties as to timing and amount of a tax increase. But starting with an assumption that fiscal events would proceed about as the staff had postulated in its deficit projections (that the requested tax increases were achieved but the spending reductions were not), it was possible to outline the alternatives to monetary policy more clearly. Such an outline must start with recognition that the Federal Government, even after the projected tax increase, proposed to absorb in its programs some $13 to $17 billion of real resources more than it absorbed from the economy through taxation. Two questions immediately arose: First, were there sufficient underutilized resources to facilitate such a program? Second, if resources must be reallocated or perhaps rationed, what role would credit policy play?

Continuing, Mr. Ellis observed that the green book noted that ". . . pressures on capacity persist in only a few lines . . ." and that ". . . capacity is continuing to expand at a rapid

pace . . . . Thus, there is ample room for expansion in output . . . ." It then stated that "For manpower, too, resources appear adequate . . . . The labor force is expected to grow rapidly, and the unemployment rate is likely to decline only moderately below the relatively low 4 per cent level."

That optimism, Mr. Ellis said, contrasted so much with the difficulty in hiring workers, especially skilled talent, generally expressed that he would like to record a different view. For example, he noted that the participation rate of the population in the labor force in the past several months had been holding at its postwar peak of between 60 and 61 per cent. Both the male and female participation rates in June were above year-ago levels and at postwar peaks. He concluded that labor force growth should not be expected to be quickly and substantially expanded by sharp increases in participation rates. Additionally, the green book commented that the rate of unemployment among adult men fell to 2.4 per cent in July, providing evidence that not much further relief could be expected from that quarter. In contrast with the staff outlook, he concluded that labor resources might fairly be termed as "tight" and not likely to be expanded sharply, especially if further increases in the armed forces were in prospect.

That conclusion led Mr. Ellis to the second question, regarding the role that credit policy should play in the inevitable

reallocation of resources necessitated by the Government program. If all Government borrowing were financed through the banks, quite surely the rationing process would occur through the price mechanism as markets responded to money demands in excess of real supply. If all Government borrowing were accomplished by sales to final investors, the rationing process would work through the credit markets in terms of rates and availability, as happened last year with its concentrated impact on housing.

Mr. Ellis' own choice between the alternative debt financing techniques, as he had postulated them, was to seek maximum feasible placement of Government debt with final investors. Markets should accept as much as they could the burden of performing the resource allocation function. Expressed another way, that probably meant that the Federal Reserve should play a game of "crunchmanship"--never allowing the market to go over the brink, but forcing bidders for investors' funds, including the Government, into full and realistic competition.

From that viewpoint, Mr. Ellis continued, the present even keel position of policy allowed the Committee to make only slow progress. But it should make some progress, and the wording of the directive as adopted at the Committee's last meeting was probably about as clear as the Committee could be in guiding the Manager.

In particular, Mr. Ellis urged that the Committee not revert to a two-way proviso clause as suggested in the staff's draft directive. The logic presented was that growth in bank credit in September could fall below the projected rate of 7 - 9 per cent. Since, as shown in the blue book, the projections implied a higher rate of growth in the bank credit proxy--as well as in the money supply--for the June-September period than for the preceding six months, he would judge that the Committee should be eager to have some shortfall from the projected rate of bank credit growth. Why should the Committee direct the Manager to seek at least a 7 - 9 per cent rate of bank credit expansion--because that happened to be the projected rate--if by reason of a strike the economy did not need such an expansion? The Committee should avoid any tendency to confuse "projections" with "goals."

Mr. Ellis remarked that the one-way proviso clause adopted at the last meeting reflected some Committee concern that bank credit and money were growing too rapidly in view of economic needs. That concern was still warranted. He urged that the one-way clause be retained as the best action the Committee could take under the dictum of even keel.

Mr. Irons reported that economic conditions in the Eleventh District were strong rather than rising substantially. Nonagricultural employment was up somewhat less than seasonally but was

higher than in June 1966. Although the number of workers had increased, labor market conditions remained tight. The District's industrial production index was rising as a result of increases in petroleum output; other components of the index were showing small gains and losses which more or less averaged out. The petroleum situation was, of course, temporary, pending the re-opening of the Suez Canal, which would probably occur when political considerations gave way to economic factors. Construction contract awards were up about 7 per cent from last year. Retail trade, as measured by department store sales, was good and although automobile sales were a bit lower than last year they also could be considered good. There was little to report on the situation in agriculture except that the District was experiencing its usual summer shortage of rain.

Mr. Irons commented that conditions at District banks could be characterized by relatively easy reserve availability and moderate demands for loans. Banks were investing in short-term securities, particularly Treasury bills and coupon issues of less than one-year maturity, in an effort to improve their liquidity positions. Demand deposits had risen recently and time and savings deposits had shown a small increase. District bankers continued to anticipate a strong fall loan demand and their reaction depended on the degree of liquid-ity they had been able to achieve. By and large, he would

characterize District conditions as relatively strong, but lacking the strength the projections for the national economy would seem to suggest.

Mr. Irons said he would not take time to comment in detail on the national economic situation. His personal assessment of the outlook was perhaps not quite as strong as that of the Board's staff; but he recognized that the expansion promised to be a strong one, even assuming a tax increase of the amount and timing recommended by the President. Rises in wages and increases in unit labor costs would have an adverse impact on the level of profits. The deterioration in the balance of payments situation was a significant factor; he shared Mr. Treiber's views on that subject.

Mr. Irons remarked that since the tax increase alone was not likely to bring about the necessary reduction in demands, monetary policy would have to complement fiscal policy in achieving restraint. He recognized that uncertainties existed at present regarding the amount and timing of the tax increase, and that even keel considerations were raised by the expected Treasury financing. Nevertheless, if there was any possibility of drifting away from the degree of ease that the Committee had been maintaining he would favor doing so. He was not proposing a basic change in policy--shifting from ease to restraint--but simply some reduction in the prevailing degree of ease. To achieve that result he thought net

free reserves in the neighborhood of $200 million would perhaps be needed, with the interest rate structure not substantially different from that prevailing.

In sum, Mr. Irons said, he would favor having the Manager take advantage of whatever opportunities arose for moving a bit in the direction of restraint, while meeting the requirements of the Treasury financing and taking account of developments with respect to fiscal policy as they unfolded. Those factors had to come first and that made the problem a difficult one. Policy should not be too tight because of the Treasury financing, but it should not be too easy because of the economic situation.

Mr. Irons added that while it was a matter of judgment he did not expect fiscal policy measures to have much effect on the economy over the remainder of this year; he thought the effects would begin to be felt in the first and second quarters of 1968. He agreed strongly with Mr. Ellis' view on the proviso clause, and favored retaining a one-way clause worded as in the current directive.

Mr. Swan remarked that economic activity in the Twelfth District continued to be satisfactory, but it was perhaps not quite as apparent in the District as in the nation that activity was about to begin expanding considerably more rapidly than at present. For example, in California and Washington manufacturing employment had

shown no change in July, with gains in aerospace employment offset by declines in nondefense industries. In California the over-all unemployment rate remained unchanged at 5.2 per cent. Prices of lumber and plywood rose sharply in July, when increases in orders coincided with low levels of production. Cash receipts of District farmers in the first five months of the year were 4 per cent below a year ago and, with the exception of wheat, crop production was expected to be somewhat lower than last year. In California the impact of the President's Federal tax proposals upon the national economy was being assessed against the background of substantial increases in State taxes that recently went into effect.

At District weekly reporting banks, Mr. Swan said, real estate loans rose further in the four weeks ending August 2, but commercial and industrial loans declined more than in the rest of the country. While most District banks still expected a substantial increase in loans by the end of the year, they indicated that current business loan demands were not particularly strong. Some of the larger banks reported recent inquiries from large corporations concerning lines of credit in the term loan area. However, such lines apparently were wanted for precautionary purposes rather than for immediate use; there had not been any substantial borrowing under them as yet.

In his judgment, Mr. Swan continued, the expected Treasury financing and the fact that the question of a tax increase was now before Congress precluded any significant change in policy at this meeting of the Committee. Along with Messrs. Ellis and Irons he favored retaining a one-way proviso clause in the directive rather than changing to a two-way clause; he saw no basis for the shift in emphasis that such a change would imply. To what had already been said on the subject he would simply add that any auto strike was likely to come quite late in the period before the Committee's next meeting. Accordingly, even if one believed that such a strike would make adoption of a two-way proviso clause desirable--a view he did not share--the action could be postponed until the Committee's next meeting.

Mr. Swan's only other comment on the draft directive related to the statement in the first sentence that ". . . economic activity is expanding more rapidly." That statement could be taken to mean either that expansion was more rapid than earlier or more rapid than had been expected. Moreover, while other statements in the first paragraph of the draft referred to past events, this statement was cast in the present tense. To meet both problems he would propose to revise the statement to read ". . . economic activity has been expanding more rapidly in recent weeks."

Mr. Galusha reported that most recent crop estimates indicated lower outputs in the Ninth District than had been expected.

For the most part, the downward revisions applied to the very dry northern half of the District's plains region. Even so, no great change from the total crop output of last year was anticipated. And it was expected that, even with somewhat lower wheat prices, total cash farm receipts would be about the same as last year. Larger numbers of cattle marketed at more favorable prices should help.

Mr. Galusha said that District construction activity had picked up remarkably in the last month or two and, with District savings and loan mortgage commitments having increased sharply through July, the near-term outlook for construction was decidedly favorable. However, and perhaps not surprisingly, the indications were that mortgage commitments had about reached a peak. With flows of funds into savings and loan associations as great as they had been, the expectation of further deposit gains could not be sustained. Word had been received recently that one large savings and loan association had decided to make no more commitments for apartment buildings. It apparently felt that residential mortgage demand would be taking all available funds, at least for a while.

Turning to Committee policy, Mr. Galusha commented that with the Treasury likely to be about to enter the market again, an "even keel" directive would seem to be indicated. Admittedly, Congress might not heed the President's call for additional tax

revenues. But he believed that it would, however tardy the action might be. Which was why, whatever the Treasury's cash position, he would urge no change in Committee targets--for the time being, anyway. But the probabilities of tardiness in Congressional action were such as to concern him; if a tax increase had to wait until the economic acceleration became fully visible to Congressional doubters, the Committee would be in an extremely awkward situation by early 1968. One day soon the Committee would have to start taking steps to condition that environment. "Instant monetary policy" might be a desirable goal, but there was no empirical evidence that the six-month gestation period had been materially shortened.

At its previous meeting, Mr. Galusha continued, the Committee had adopted what could be described as a one-way proviso clause. He had not objected, but only because of a certain diffidence. A proviso clause might make sense, although he continued to have his doubts. There would appear to him to be no good reason, however, for ever having a one-way proviso clause. It would seem to make little sense to limit the contingencies to which the Desk might respond once the decision was made to recognize any; the "exclusio" doctrine of the legal draftsman might well be kept in mind. The suggestion that a less-than-expected increase in bank credit--however unlikely it might have been--was of no concern to the Committee

would seem unfortunate, particularly if one of the Committee's major audiences was posterity. He would, therefore, urge that the Committee go back to the usual two-way clause if a proviso was included at all. It should instruct the Manager to alter the free reserves or interest rate targets--to the extent, of course, that the Treasury financing permitted--if the increase in bank credit was turning out greater or less than was expected.

Mr. Scanlon commented that a general consensus had developed in the Seventh District that the economy had regained momentum. Widespread agreement existed, moreover, that prospective Government and private spending would press increasingly against available resources. New wage contracts had been increasingly generous and many firms found that their markets permitted at least a portion of higher costs to be recaptured through price increases. As a result, with a few exceptions, business sentiment strongly favored a tax increase approaching the magnitude requested by the President. While there was strong support among District businessmen for reductions in Government spending, it was generally assumed that they would not be made in any significant volume and that a tax increase was the only feasible means of avoiding excessively restrictive monetary policy.

The tendency for unemployment to rise in District centers apparently had been arrested, Mr. Scanlon said. Surveys of employer

hiring intentions indicated increases in employment in most centers in the months ahead. The Michigan situation would improve rapidly as full scale production of 1968 autos began, barring, of course, an extended strike. Steel producers with whom he had talked now were experiencing a moderate rise in their orders on a broad front, and they expected that uptrend to continue through the year. An increase in ordering could cause lead times for industrial raw materials and components to stretch out again. Such a development, along with widespread expectations of price increases, could alter expressed intentions of purchasing agents to reduce inventories further.

Mr. Scanlon went on to say that while farm equipment sales had been about on a par with last year and less than expected, output of most major appliances was rising again after production cutbacks that proved to be excessive for some firms. Construction contracts were up 30 per cent from last year in the Midwest in June, compared to a 12 per cent rise for the nation; the six-month deficit in construction contracts was reduced to 3 per cent in the Midwest and 5 per cent in the nation. Mortgage funds, construction labor, and materials were in ample supply. But labor costs and materials prices were rising. The major deterrent to a faster rise in construction activity appeared to be delays in the acquisition and development of land.

Mr. Scanlon remarked that record crops were expected to cause reduced prices and, therefore, lower income from sales of crops in the District this year. Income from livestock, on the other hand, might exceed the year-ago level in the second half.

Major District banks had effectively avoided the discount window in recent weeks, Mr. Scanlon observed, satisfying their funds needs in the market. The banks had also altered their market strategy somewhat, obtaining relatively fewer funds through net Federal funds purchases and more through aggressive marketing of CD's. CD's outstanding at Chicago banks on August 2 were at a record level, as was true also for the country as a whole.

As to policy, Mr. Scanlon believed it would be desirable for the Committee firmly to slow the expansion in money and credit, and were it not for Treasury financing activity he would favor moving to a policy of somewhat less ease or to a more neutral monetary policy. In view of the financing, however, an even keel policy seemed imperative. He found the draft directive generally acceptable but, like most others who had spoken so far, he would prefer today to employ a one-way proviso clause similar to that in the current directive rather than the two-way clause proposed in the draft directive, although he was not opposed to a two-way proviso under certain conditions. He interpreted the term "current expectations" in the proviso clause as being the expectations noted in the blue book.

Mr. Clay remarked that accumulating evidence on both the private and the public sectors of the economy underscored the need for a lesser degree of public policy stimulation. Encouragement could be derived from the President's request for an income surtax. What the Congressional action would be and on what scale and timing action might be taken was, of course, not known.

While enactment of the President's proposal would be very helpful and would facilitate the formulation of monetary policy, Mr. Clay continued, there was room for considerable concern over the expansiveness of recent monetary policy. The Committee needed to find a way to shift to a slower rate of bank credit growth. There was a risk that on a period-by-period basis the Committee would continue to expand the reserve base beyond what it preferred to do. That risk was particularly related to the amount and frequency of Treasury financing and its impact upon monetary policy formulation and implementation.

Mr. Clay acknowledged that there were problems associated with such a move in view of the continuing large demands upon the credit markets and the existing high level of interest rates. One was the Treasury's large financing job in itself. Another was the desire to avoid any appearance of not fully cooperating with the Administration's effort to bring about a better balance between fiscal and monetary policy. A third was a concern over possibly

producing an adverse impact upon the flow of funds among financial institutions. However, moderate reduction in credit expansion probably would not be incompatible with any of those objectives.

For the immediate future, Mr. Clay said, the Committee again was somewhat limited in its action by Treasury financing, which suggested the desirability of maintaining prevailing money market conditions. Under those conditions, staff projections for September pointed toward bank credit expansion at an annual rate of only 7 to 9 per cent, which would be highly desirable. The staff also indicated that there was a considerable degree of uncertainty surrounding those projections. If bank credit should appear to be expanding at a faster pace, some firming of money market conditions should be permitted.

The draft economic policy directive appeared to be satisfactory to Mr. Clay.

Mr. Heflin commented that Fifth District business exhibited less evidence of renewed expansion than was found in the national data. The Richmond Reserve Bank's latest survey indicated little change in manufacturers' new orders and inventories, with further easing of the order backlog. The textile industry experienced a flurry of activity two or three weeks ago but that now appeared to have been due entirely to buyer stockpiling in anticipation of price increases which were announced last week. A sizable decline in

building permits in June introduced some uncertainty about the strength of the recovery in construction. On the other hand, the mild downtrend in nonagricultural employment and in manufacturing manhours had been arrested, if not reversed, and furniture makers reported good progress in bringing inventories under control. Business loan demand appeared less strong in the District than in the nation, and some of the bankers expressed doubts that demand would pick up significantly in the near future. Despite the rather spotty current picture, the optimism index was at the highest level since early last year.

In connection with the comments today on the probable strength of loan demands, Mr. Heflin reported that there had been a substantial increase recently in the number of calls received at the Richmond Bank from District bankers interested in discussing that question. They seemed to be highly uncertain on the subject, and it was his impression that they were resolving their doubts on the side of expectations of a weak loan demand. For the first time in recent months, in the Reserve Bank's latest survey businessmen had been more optimistic than bankers. He was not sure what that signified, but he was confident that bankers were reasonably sure that the loan demands they would experience would not approach the proportions of last year.

With respect to the national economy, Mr. Heflin continued, the latest data left little doubt that a renewal of the expansion was under way; the question was at what rate it would proceed. Nevertheless, given the lags involved in monetary policy, the current advance and the prospect of continuing expansion of government and private demands suggested to him the desirability of a slowdown in the recent rapid growth of reserves, credit, and money. Moreover, the reports the Committee had heard this morning on the balance of payments suggested that policy should be shaded toward restraint. But even keel considerations and the imminence of a restrictive tax increase that bore the Committee members' endorsement argued against any major change in the posture of policy. That was especially the case in view of the highly volatile pattern of expectations that had characterized the financial markets lately.

Mr. Heflin believed that over the next few weeks policy should be directed primarily at moderating any exaggerated rate movements that might develop. The blue book suggested that existing money market conditions were consistent with rates of growth in the aggregateswell below those of earlier in the year. He hoped that would prove a correct assessment. He would be prepared, however, to accept temporary growth in the aggregates at rates faster than projected if that was necessary to preserve orderly markets.

Mr. Mitchell said that in his judgment the Committee's present policy was about right. It was tinged with some concern about excessive rates of growth in monetary variables, which he thought was appropriate. Accordingly, he would not want to change policy significantly at this juncture.

Turning to the directive, Mr. Mitchell said he would favor a one-way proviso clause like that in the existing directive. If he were to make any suggestion for change, it would be to add a proviso to that proviso, to the effect that in the event bank credit expansion exceeded expectations and Desk operations undertaken to restrain it resulted in disintermediation, the Desk should move the other way. However, from Mr. Axilrod's remarks he concluded that although the matter was close disintermediation probably would not be a major problem in the month ahead. Disintermediation could be significant if the Treasury offered a particularly attractive security in the forthcoming financing, but there was not much the Committee could do about that. He concluded that the Manager was likely to have sufficient room for maneuver in the coming period to warrant instructing him to pull back somewhat if monetary expansion was faster than desirable.

Mr. Mitchell added that it appeared that a fiscal program to supplement monetary policy, which the Committee had favored for some time, finally was about to be adopted. For that reason he

would favor recasting the statement of the Committee's general policy in the last sentence of the directive's first paragraph. He suggested a sentence reading, "In this situation, it is the policy of the Federal Open Market Committee, as fiscal policy proposals are being considered by Congress, to avoid as far as possible a deterioration in the financial environment and expectations due to excessive money and credit expansion."

Mr. Daane said that the latest information on the domestic economic situation--which Mr. Brill had said made pleasant reading--coupled with the unpleasant report on the balance of payments would have inclined him to the view, other things equal, that the Committee's operations should be directed toward gradually attaining somewhat less ease. As had been generally recognized in the discussion today, however, other things were not equal; the Administration's tax program was being considered by Congress, and a Treasury financing lay ahead. Accordingly, he concurred in the view that the Committee should not make a basic change in policy at this time.

With respect to the draft directive, Mr. Daane said that he would favor Mr. Treiber's suggestion with respect to the balance of payments sentence. And, like Mr. Mitchell, he questioned the desirability of retaining the last sentence of the first paragraph in its present form. In his judgment the sentence was not compatible

with the preceding text of the paragraph describing the more rapid domestic expansion and the serious balance of payments problem. He would favor recasting the final sentence to read "In this situation, it is the policy of the Federal Open Market Committee to foster financial conditions, including bank credit growth, conducive to noninflationary economic expansion, recognizing the need to avoid developing inflationary pressures and to retain reasonable price stability for both domestic and balance of payments purposes."

In the same vein, Mr. Daane said, he would change the second paragraph of the staff's draft to read "To implement this policy, and taking particular account of the expected Treasury financing activity, System open market operations until the next meeting of the Committee shall be conducted with a view to maintaining about the prevailing conditions in the money market." The discussion of the proviso clause today suggested to him that it would not be advisable to include such a clause in the directive, particularly if the emphasis in the period ahead was to be on maintaining an even keel. But if any modifying clause were to be added, he would suggest one reading, ". . . but operations shall be modified if necessary, insofar as Treasury financing activity permits, to moderate the recent rate of increase in bank credit." He also favored giving the Manager full flexibility to engage in coupon operations--and even some encouragement to undertake such operations

under circumstances like those Mr. Holmes earlier had indicated he would consider appropriate.

Mr. Daane then reported briefly on developments at recent Group of Ten meetings concerned with international monetary reform. He noted that a meeting of the Ministers and Governors of the Ten, which Chairman Martin and Secretary of the Treasury Fowler had attended, had been held in London on July 17 and 18. Most of the discussion had concerned the two issues of decision making and the repayment provisions that should be associated with the new asset. The discussion was inconclusive, although it appeared at one point that the Group was moving toward a package involving an 85 per cent requirement for decision making, an average-use formula for reconstitution of the asset, the name of "special drawing right," and acceptance of holding limits on the new asset of perhaps three times the initial allocation.

Subsequently, Mr. Daane continued, the Deputies had met in Paris on July 27 and 28. They reviewed the whole draft scheme that had been developed originally by the Fund staff on a facility for creating reserve drawing rights. It became apparent at that meeting that the flexibility which the French had evidenced to a degree at the London meeting was somewhat illusory. As he read the situation the issues were still open, and remained to be resolved by the Ministers and Governors at their meeting in London on August 26 and 27. Chairman Martin, Mr. Solomon, and he would attend that meeting.

Mr. Maisel thought the Manager should be congratulated for the fact that in the past period there was a minimum of market intervention. The day-to-day variations at times loomed large, but they did no harm to policy or future goals. That might well be an indication that the market could be allowed more variance in reserves, with intervention occurring primarily when reserves had to be furnished or subtracted in order to achieve definite policy goals. The trade-off between actual intervention and clearer public statements of policy should be explored.

The Committee was entering an even-keel period, Mr. Maisel noted. But even if there were no Treasury financing, a policy of no change would be proper. He would prefer to have the proviso clause omitted from the directive to be issued at this time; and, if it were retained, to have its limits considered to be as wide as possible.

The Committee should, meanwhile, use this time to look toward the future and try to improve its dialogue for periods ahead, Mr. Maisel said. Both at the previous meeting and today he had been concerned about some of the statements made. It seemed to him that some of the guideposts staked out were looking backward and failed to consider the Committee's desired goals for the economy while stressing too simple concepts of money flows. He thought the Committee should be concerned, but it should be clear as to what dangers might appear.

What lessons could the Committee derive from the current credit situation? Obviously, Mr. Maisel said, it was necessary to consider movements in the banking system, in the over-all financial markets, and in related interest rates. When one examined the total monetary flows for the first half of the year, one noted that they were a good deal lower in absolute terms than in the past two years. In relation to the GNP, the amount of credit raised in the financial markets so far this year had been relatively a good deal below that borrowed on the average over the past six years.

That depressed rate of financial flows, Mr. Maisel continued, was reflected in rates of interest which by any traditional pattern could only be characterized as extremely high. Those rates of interest appeared surprising when one recognized that the current flows had been accompanied by a growing amount of intermediation and a decrease in direct lending. With flows going back through financial institutions, lower not higher interest rates should be expected. It would appear that expectational factors and a shift in liquidity desires had been extremely important in recent markets.

Looking forward in terms of the projections of both the flow of funds and GNP, Mr. Maisel noted that increased borrowing was expected, but almost entirely because of the Government deficit. In contrast to the credit flows, the Federal deficit on a national

income accounts basis was not expected to be as large as in the past six months even though it would require a larger amount of Government borrowing. Even with the large increases in Government spending, the continued deficit on a national income accounts basis, and the expected shift in inventories, total demand for goods in this fiscal year was not expected to expand faster than supply. Even with projections showing a large increase in spending by the end of the fiscal year, the capacity utilization rate would still be somewhat lower than a year ago.

As to the present implications of those projections for monetary policy over the next six months, Mr. Maisel first noted that large credit flows were implicit in the projection of real GNP, called for through a growing amount of intermediation. As a result, their size need not, per se, be a particular matter of concern. To be troubled by them, the Committee would have to find that they were affecting total demand in an unsatisfactory way. He was somewhat, but not too, surprised--since these tend to be value judgments--at those who felt that the Committee should be satisfied with the current relationships of supply and demand. A second implication was that, while the current exceedingly high rates of interest might or might not create problems, the economy would probably be improved if the needed flows could be obtained with lower rates. There would be a more satisfactory situation with respect to both the distribution of the demand for goods and the distribution of income.

Given balanced projections of supply and demand, Mr. Maisel continued, what did the fear of an excess creation of credit seem to be based upon? What assumptions appeared to underlie the concern over the rate of creation of credit? Such concerns appeared to minimize the need for large credit flows to rebuild the liquidity that existed in the system a year ago. They also seemed to assume that there should be a continued decrease in the ratio of credit to real output in the economy. Was it likely that a continued decrease in the ratio of money to GNP should take place, given the desire for liquidity which the experience of last year built up in many minds? Those concerns also appeared not to consider the high interest rates as any measure of the supply and demand situation. Finally, they seemed to imply that current flows might be a danger because they would make it impossible to halt bank credit expansion at some time in the future if that became desirable.

He must admit, Mr. Maisel said, that he did not agree with most of those assumptions. It seemed clear to him that much higher levels of credit flows should be expected over the next six months, both because much of the increased demand would continue to come through the Government deficit and because--given the experience of last year--it should be expected that many parts of the economy would want to operate with considerably higher levels of liquidity. Thus, it was entirely possible that the current high flows with

high interest rates reflected not only a current shortage of liquidity but also too little liquidity for the future.

Also, it seemed to Mr. Maisel that the concern over future expansion of credit neglected the lessons of this past year. It had been demonstrated that, if the System wanted to react, it was possible for it properly to restrict the level of credit creation. There was no necessary relationship between the amount of credit created now and the amount of credit to be created next year. What the Committee should concentrate on was making certain that the amount of credit created over the next six months would insure an availability of funds and interest rates that would allow the economy to match a growing supply and demand in various sectors. The Committee had no indication that such a matching in a period of expansion could be related directly to any specific rate of expansion of money or bank credit. In particular, there was no indication that the current expansion rates were creating any future problems.

Mr. Maisel concluded that the Committee must continue, to the best of its ability, to attempt to measure the influence that credit creation, availability of funds, and interest rates were having on the real flows of supply and demand. The excesses or shortfalls of demand in particular sectors should be the Committee's policy guides, not any particular set of credit or monetary numbers which might seem high or low in comparison to past periods.

Mr. Brimmer noted that both Mr. Reynolds and Mr. Treiber had suggested in their remarks on the balance of payments that further tightening was needed in the voluntary program administered by the Department of Commerce to limit direct investment abroad. He agreed, but would suggest that the part of the foreign credit restraint program administered by the Federal Reserve should also be examined. According to estimates the Commerce Department recently had made at his request, in 1966 financial institutions accounted for $380 million, or about 12 per cent, of the $3.4 billion of total direct investment outflows. The $380 million figure included $50 million of direct investments by banks, $60 million by insurance companies, and $270 million by other financial institutions. While not large, direct investments by banks were growing--it appeared that in 1966 they were more than double the level of a few years ago--and he inferred from the data that other financial institutions also were stepping up their direct investments. He thought the System should give some thought to improving its guidelines for financial institutions, perhaps by making them more nearly comparable to the Commerce Department's guidelines for nonfinancial corporations.

Mr. Brimmer then observed that he was disturbed by the Manager's suggestion that the Treasury would be well advised to offer a long-term note with a 5-1/2 per cent coupon in the forthcoming cash financing. In his judgment that would be an unfortunate step on two grounds. First, a 5-1/2 per cent coupon might well trigger

disintermediation. Secondly, it was desirable for the Treasury to mesh debt management policy with fiscal and monetary policy. The Manager had suggested that a 5-1/2 per cent note might help improve the tone of the market, but it would represent poor debt management in that it would put some upward pressures on the rate structure. Thus, he would not favor urging the Treasury to take advantage of its present freedom to sell a long-term note.

Turning to the directive, Mr. Brimmer noted that the Committee had been advocating a better meshing of monetary and fiscal policy for some time. Accordingly, he thought it highly desirable to include a statement of the Committee's general policy in the first paragraph along the lines of that suggested by Mr. Mitchell. He favored deleting the proviso clause entirely because of present uncertainties about the probable rate of bank credit growth, as reflected in the wide differences between the Board and New York Bank projections. He shared Mr. Daane's views with respect to operations in coupon issues.

In a concluding observation Mr. Brimmer said he thought the Board and the Reserve Bank Presidents should give serious consideration to a restructuring of bank reserve requirements. There would have been an opportunity to do so in early September when, according to the blue book, the System was expected to be supplying reserves, but that chance had been missed. He hoped that System people would consider the subject actively, looking toward the next opportunity in November.

Mr. Robertson commented that he was glad Mr. Brimmer had raised the matter of the System's guidelines for financial institutions under the voluntary foreign credit restraint program. That subject was under active consideration at present.

Mr. Sherrill said he thought the most important consideration at present was the fiscal program now before Congress. The Committee's major objective should be to encourage Congress to enact that program, since the inflationary pressures that could be expected later in 1967 and in early 1968 were likely to be too strong to be dealt with by monetary policy alone. Accordingly, he did not believe that this was the time to change the stance of monetary policy.

Having expressed that view, Mr. Sherrill continued, he would like to pause for a moment to consider the other side of the coin--namely, that tax increases of the recommended amount and timing might well have a highly deflationary effect on the economy, indirectly by influencing psychology as well as directly. In his judgment that possibility had not been sufficiently considered. In any case, he thought the Committee's decision on whether to begin shifting toward more restraint in monetary policy should await clarification of the nature and effects of the fiscal program.

Mr. Sherrill said he found the directive as drafted by the staff to be acceptable. He would prefer a two-way proviso clause

because any shortfall of bank credit growth below the projected range was likely to be due to an auto strike, and he would not consider it desirable for the System to reinforce the economic and psychological effects of a strike by appearing to be tightening monetary policy.

Mr. Sherrill thought there probably would not be much opportunity for operations in coupon issues during the coming period. He felt, however, that such operations should be kept in mind as an important tool available for use by the Desk, and he agreed with the Manager's description of the circumstances under which their use would be appropriate.

Mr. Hickman observed that economic activity was showing increasing signs of improvement along a broad front, as had been expected. Given the progress already made in the correction of business inventories, industrial output should turn upward this quarter--indeed, it already had--and the pace of economic activity generally should quicken. That was corroborated by strengthening in a number of leading indicators, including durable goods' new orders and backlogs, machinery orders, building contracts, hours worked per week, and so forth. On the other hand, the likelihood of important gains in plant and equipment spending for the rest of the year was still doubtful because of excess capacity and shrinking profit margins.

Mr. Hickman remarked that not surprisingly, in view of the high cyclical sensitivity of the Fourth Federal Reserve District and moderate secular growth, business in the area had lagged the recent improvement in the nation. Manufacturing activity, construction, retail sales, and employment remained sluggish. On the other hand, preliminary results of the Cleveland Reserve Bank's latest survey of District manufacturers showed widespread expectations of strengthening in orders, shipments, backlogs, and employment. The steel industry, in particular, was optimistic about shipments for the remainder of the year.

Turning to policy, Mr. Hickman noted that the Committee's leeway for action over the next four weeks was limited because of Treasury financing. However, he continued to be disturbed about the very large figures for bank reserves and credit projected for the month of August as a whole, coming on top of the huge expansion in July--although he was, of course, aware of the intra-month weakening during August. While the System had to accommodate the Treasury up to a point, it appeared to be supplying more reserves than seemed desirable in light of emerging economic pressures--even with the proposed surtax on personal and corporate income. Therefore, he reiterated his recommendation that rates of growth in aggregate reserves and bank credit should be constrained to an upper limit of 6 to 8 per cent. That could be a real problem in

September if private loan demand for inventory and tax payment purposes expanded markedly, as the blue book suggested was a possibility and the New York Reserve Bank appeared to think likely. If private demand strengthened and the Committee provided less reserves than the amount required to accommodate that strengthening, interest rates would rise, and a modest amount of disintermediation might result; but that would not be undesirable if it eliminated the need for a sharp reversal in policy later on. For reasons indicated by Mr. Ellis and others, he preferred the one-way proviso clause and would revise the staff's draft directive accordingly.

Mr. Bopp remarked that the Board's staff had presented an impressive case for a strong upturn with inflationary overtones during the rest of the year. In the Third District, perhaps partly because he was looking at older information, the signs were a bit more mixed. Thus, although employment remained exceptionally high, unemployment rates continued to rise. Manufacturing output dropped in June for the second month, as did steel production. On the other hand, construction contracts and automobile registrations were up.

In the financial sector, Mr. Bopp observed, developments were more similar to the national scene. Large commercial banks in Philadelphia had experienced about the same rate of expansion as their counterparts throughout the nation. In July, business

loans moved up to seasonal peaks and consumer loans increased further. Banks had added substantially to their holdings of Government securities, while reducing holdings of other securities slightly.

Because of continuing concern with the threat of disintermediation, Mr. Bopp said, last week the Philadelphia Reserve Bank again surveyed mutual savings banks and savings and loan associations in the Philadelphia area. The officers talked with were cautiously optimistic. Rebuilding of liquidity positions seemed either to be proceeding satisfactorily or to be well nigh complete. Most officers interviewed expected an inflow of funds to continue; some looked for a growth of 8 to 12 per cent over 1966. One officer, however, saw some signs of disintermediation, and savings banks had some concern as to the volatility of funds invested in their certificates. Several of those interviewed indicated that they were watching deposits closely in order to determine the impact of the 5 per cent certificates guaranteed for 10 years which one commercial bank had reintroduced in mid-July.

Mr. Bopp commented that the President's announcement of his decision to seek a 10 per cent tax surcharge apparently had allayed fears of a repeat of the 1966 credit crunch. That was borne out in the Reserve Bank's survey. Thus, even though some of the officers surveyed feared that a tax increase of that size

would hurt savings inflows, none anticipated being caught in the same squeeze for funds this year as last.

Much as he approved the announcement about taxes, Mr. Bopp felt that that development did nothing to relieve the problems now facing monetary policy and that it might not be of much help for some time. Pressures on financial markets were still intense. Judging by the behavior of interest rates, much of the impact of the tax announcement had already been discounted. Moreover, official disclosure of the likely size of the deficit, even given a tax increase, had demonstrated again that the Treasury would be a large demander of funds. And corporate and municipal calendars for the next month, while down, were still substantial.

Mr. Bopp thought that the dilemma for policy in the months ahead was likely to be one of moving away from the present posture of ease while minimizing the risk of disintermediation that still higher interest rates could cause. A complicating problem would be the almost constant presence of the Treasury in the market.

Even keel considerations would prevail for most of the period between now and the next meeting, Mr. Bopp noted. That would not present much of an immediate problem in view of the fact that the economy was still in transition from a slow first half to a faster second half of the year, with the speed and strength of the recovery still in doubt. Looking to the future, however, if

the projections in the green book proved to be accurate, a need to move toward a less easy monetary policy and even keel considerations would increasingly conflict. Ideally, for economic reasons and because advocacy of fiscal action might have created a general belief that monetary restraint would not be used, a move toward less ease should be gradual. But given the persistence of Treasury needs, it might be necessary for the Committee to move rather abruptly when the opportunity arose.

Mr. Patterson observed that economic information becoming available since the last meeting of the Committee suggested to him that, although the stage continued to be set for a resumption of a vigorous expansion, some actors in the economic drama had not yet speeded up the action. In the Sixth District, for example, there were further signs that the downward trend in manufacturing employment had ended and might be leveling off. Nevertheless, most areas of the District reported few significant changes in jobs other than increases in Government employment and in strike-affected activities. The labor supply in most major labor market areas of the District was characterized as being "adequate" in contrast with the tight conditions of six months ago. In construction there was promise of future expansion, with June producing the highest dollar volume of contracts since November

1966, but construction employment had not yet increased. However, there was evidence that consumer spending had picked up, with automobile sales buoyant in June and July.

Mr. Patterson felt sure that the easier monetary and credit policy the Committee had been following had helped to set the stage for the revival. He was not sure, however, that having helped set the stage there was much more the Committee could do at the moment to promote revival until nonmonetary forces or forces outside the area of the System's influence could take over. Meanwhile, there was a clear danger that the Committee might at this point do too much.

Certainly, Mr. Patterson continued, it could not be said that the banking system was in a tight situation. Thus, if the Committee continued to tie its policy to maintaining money market conditions, there seemed to him to be a danger that it might be trapped into promoting a more rapid expansion in bank credit than might be compatible with sustainable recovery and price stability. Consequently, he had been pleased to have the proviso clause included in the instructions given to the Desk at the last meeting. He would hope that it would be included in the instructions issued at this meeting.

The rates of bank credit expansion for July and August seemed to Mr. Patterson to be too high. Even keel considerations

probably dictated a goal of maintaining about the prevailing conditions in the money market until the next meeting of the Committee. Therefore, he was pleased to note that the current projection of the expansion rate in the bank credit proxy for September consistent with maintaining money market conditions was substantially lower than the rates for July and August.

Mr. Patterson favored the directive as written with Mr. Treiber's suggested amendment to the statement concerning the balance of payments and a return to the one-way proviso clause of the directive issued on July 18.

Mr. Lewis observed that the economy had been operating at a generally high level and appeared to be gaining strength. Final sales rose at a rapid 8 per cent rate from the fourth quarter of last year to the second quarter of this year. That rate, which was incompatible in the long run with reasonably stable prices, approached the unsustainable 10 per cent rate of the period from late 1964 to early 1966. Employment had remained strong and upward pressures on prices appeared to be mounting.

Mr. Lewis was encouraged by the President's recent tax proposals and thought they were a step in the right direction. Assuming those proposals were adopted, the estimates of the St. Louis Reserve Bank still indicated a sizable deficit in the

high-employment budget for the period from the fourth quarter of 1967 through the first half of 1968. The estimated deficit, which would be about half the probable deficit in the absence of a tax increase, implied a very stimulative fiscal situation.

In any case, Mr. Lewis continued, the actual magnitude and timing of the bill which would be passed by Congress were not known. The final bill, which might provide less restraint than the current proposals, would not affect tax payments before the fourth quarter of this year. The major impact of increased taxes on economic activity might occur only after a significant lag.

Consequently, Mr. Lewis thought that a continuation of the high rates of monetary expansion prevailing in the past six months would be undesirable. While the rates of growth of Federal Reserve credit, total reserves, and bank credit had been less rapid over the past few months than earlier in the year, they remained relatively high. He was particularly concerned about the accelerated growth of other measures--reserves available for private demand deposits, money, and money plus time deposits. He was submitting a table for the record in which the growth rates in those magnitudes over the past three months were compared with the rates in the preceding three months and in some recent trend periods.[1/]

1/ Appended to this memorandum as Attachment B.

Mr. Lewis concluded by saying that in view of the strengthening economy, upward pressures on prices, prospects for excessive total demand, and balance of payments considerations, he would prefer to see the rate of monetary expansion become much more moderate in the next few months.

Mr. Robertson then made the following statement:

> This seems to me to be a time when we clearly want to keep monetary policy on a steady course. The expected Treasury financing announcement may involve a coupon issue, and calls for "even keel" on technical grounds. But the President's fiscal program seems to me to be the overriding consideration. As proposed, it is a strong program, and one which, if enacted, will bring to the fore serious considerations with respect to the mix of fiscal and monetary policies. In the meantime, while the proposal is moving forward, it seems incumbent on us to keep financial markets from becoming either too tight or too loose, so that we do not prematurely prejudge the nature of the fiscal program or its effects; we can move appropriately when we are better able to gauge the progress of the program and the reactions of businesses, consumers, and investors to it.
>
> I do not mean to be saying that our stance toward financial markets should be completely rigid. I continue to think that we need the minimum flexibility that is implied in a proviso clause referring to bank credit that is two-way--not one-way. It is only prudent. A two-way proviso does not prevent some tightening of money market conditions if bank credit begins to expand more rapidly than appears desirable, but a one-way proviso as we used at the last meeting does prevent some easing if bank credit begins to show unexpected sizable weakness. With a fiscal program of restraint proposed, I do not think we want to appear insensitive to a significant weakening in bank credit, no matter how improbable one may think such weakness.
>
> Also, the economic outlook is not so certain as to incline me toward a one-way worry about bank reserves and credit developments. To be sure, we have more news

pointing to an economic upswing now than we had last time--industrial production and retail sales, to mention two of the most prominent. But signs of real economic revival are in themselves cause for satisfaction and not for concern. It is, of course, the growing price pressures and persisting balance of payments problem that are most worrisome in the situation. As time goes on, we may have to shape over-all monetary policy to put more stress on those problems, but we will have to do it in the light of the fiscal program that emerges, in the light of the susceptibility of price pressures to monetary action, and perhaps even in the light of the need to assure a declining unemployment rate in the economy as an aid to combatting social unrest in the country.

Mr. Robertson then remarked that the members of the Committee seemed to be in fairly close agreement today on the principal matter--that "even keel" represented the appropriate course for policy--although divergent views had been expressed regarding the proviso clause and a number of suggestions had been made for changes in other parts of the draft directive.

After discussion the Committee agreed to accept the revisions in the first paragraph of the draft directive proposed by Messrs. Treiber and Swan, and to use a one-way proviso clause referring to bank credit in the second paragraph.

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

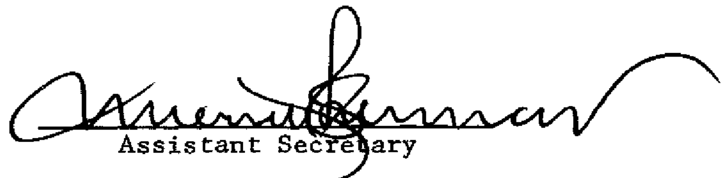
The economic and financial developments reviewed at this meeting indicate that economic activity has been expanding more rapidly in recent weeks. With strengthening of private demands for final products and further curtailment of inventory investment, a better balance between

inventories and sales is emerging. Upward pressures on costs persist and the over-all indexes of both wholesale and consumer prices have risen further. The balance of payments deficit has remained substantial and is a serious national problem. Bank credit expansion has continued large, while most short- and long-term interest rates have fluctuated close to their highs of the year, under the combined pressure of heavy private security market financing and of current and prospective Federal financing. A new fiscal program has been proposed by the President, including a sizable increase in income taxes, which would make a substantial contribution to balanced economic growth. In this situation, it is the policy of the Federal Open Market Committee to foster financial conditions, including bank credit growth, conducive to continuing economic expansion, while recognizing the need for reasonable price stability for both domestic and balance of payments purposes.

To implement this policy, while taking account of expected Treasury financing activity, System open market operations until the next meeting of the Committee shall be conducted with a view to maintaining about the prevailing conditions in the money market; but operations shall be modified, insofar as Treasury financing permits, to moderate any apparent tendency for bank credit to expand more than currently expected.

It was agreed that the next meeting of the Committee would be held on Tuesday, September 12, 1967, at 9:30 a.m.

Thereupon the meeting adjourned.



Assistant Secretary

ATTACHMENT A

CONFIDENTIAL (FR) August 14, 1967

Draft of Current Economic Policy Directive for Consideration by the Federal Open Market Committee at its Meeting on August 15, 1967

The economic and financial developments reviewed at this meeting indicate that economic activity is expanding more rapidly. With strengthening of private demands for final products and further curtailment of inventory investment, a better balance between inventories and sales is emerging. Upward pressures on costs persist and the over-all indexes of both wholesale and consumer prices have risen further. The balance of payments deficit has remained substantial. Bank credit expansion has continued large, while most short- and long-term interest rates have fluctuated close to their highs of the year, under the combined pressure of heavy private security market financing and of current and prospective Federal financing. A new fiscal program has been proposed by the President, including a sizable increase in income taxes, which would make a substantial contribution to balanced economic growth. In this situation, it is the policy of the Federal Open Market Committee to foster financial conditions, including bank credit growth, conducive to continuing economic expansion, while recognizing the need for reasonable price stability for both domestic and balance of payments purposes.

To implement this policy, while taking account of expected Treasury financing activity, System open market operations until the next meeting of the Committee shall be conducted with a view to maintaining about the prevailing conditions in the money market; but operations shall be modified, insofar as Treasury financing activity permits, to moderate any apparently significant deviations of bank credit from current expectations.

ATTACHMENT B

SELECTED MEASURES OF MONETARY DEVELOPMENTS

Compounded Annual Rates of Change

	April 1967 July 1967	January 1967 April 1967	January 1967 July 1967	1964-1966	1960-1964
Bank Reserves (Adjusted for changes in reserve requirements)					
Federal Reserve holdings of Government securities	+ 8.0	+ 23.7	+ 15.6	+ 9.3	+ 8.1
Total reserves	+ 6.7	+ 12.5	+ 9.6	+ 4.4	+ 3.7
Reserves available for private demand deposits	+ 15.6	+ 2.9	+ 9.0	+ 2.7	+ 1.6
Money					
Money Stock	+ 12.3	+ 6.0	+ 9.1	+ 4.2	+ 2.6
Demand deposit component	+ 14.8	+ 5.9	+ 10.3	+ 3.8	+ 2.3
Currency component	+ 4.2	+ 6.4	+ 5.3	+ 5.8	+ 3.7
Time deposits	+ 16.4	+ 19.4	+ 17.9	+ 13.6	+ 14.7
Money stock plus time deposits	+ 14.3	+ 12.4	+ 13.3	+ 8.4	+ 7.0

	April 1967 July 1967	January 1967 April 1967	January 1967 July 1967	1964-1966	1960-1964
Bank credit					
Board proxy	+ 10.3	+ 14.2	+ 12.2	---	---
End-of-month series	+ 9.6	+ 14.1	+ 11.8	+ 9.3	+ 7.9
St. Louis daily average series	+ 9.8	+ 15.1	+ 12.5	+ 8.9	+ 7.8