A meeting of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System in Washington on Tuesday, January 11, 1955, at 10:45 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Sproul, Vice Chairman
Mr. Balderston
Mr. Bryan
Mr. Leedy
Mr. Mills
Mr. Robertson
Mr. Szymczak
Mr. Williams
Mr. C. S. Young

Mr. Riefler, Secretary
Mr. Thurston, Assistant Secretary
Mr. Vest, General Counsel
Mr. Thomas, Economist
Messrs. Bopp, Roelse, and R. A. Young, Associate Economists
Mr. Rouse, Manager, System Open Market Account
Mr. Carpenter, Secretary, Board of Governors
Mr. Sherman, Assistant Secretary, Board of Governors
Mr. Miller, Chief, Government Finance Section, Division of Research and Statistics, Board of Governors
Mr. Gaines, Securities Department, Federal Reserve Bank of New York

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

Messrs. Erickson, Powell, and Irons, Presidents of the Federal Reserve Banks of Boston, Minneapolis, and Dallas, respectively

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the Federal Open Market Committee held on December 7, 1954, were approved.

Upon motion duly made and seconded, and by unanimous vote, the actions of the executive committee of the Federal Open Market Committee as set forth in the minutes of the meeting of the executive committee held on December 7, 1954, were approved, ratified, and confirmed.

Before this meeting there had been sent to the members of the Committee a report of open market operations prepared at the Federal Reserve Bank of New York covering the period December 7, 1954, to January 6, 1955, inclusive, and at this meeting there was distributed a supplementary report covering commitments executed January 7 to January 10, 1955, inclusive. Copies of both reports have been placed in the files of the Federal Open Market Committee.

Upon motion duly made and seconded, and by unanimous vote, the open market transactions during the period December 7, 1954, to January 10, 1955, inclusive, were approved, ratified, and confirmed.

Mr. Young made a statement with respect to the current economic situation, presenting substantially the information contained in a staff memorandum distributed under date of January 7, 1955. He said that the upturn in economic activity, dramatized by the 3 point rise in November in the index of industrial production, had been confirmed by a further rise for the December index probably amounting to 2 points, and by a broadening of expansive indications to a wider range of activities and markets. Substantial recovery in industrial activity and further expansion in record levels of construction have been accompanied by moderate strengthening of prices of a number of industrial and building materials.

Prices of most finished goods at wholesale have generally continued stable, while prices of goods in retail markets have continued to ease somewhat under the influence of ample supplies and intensified competition. Mr. Young noted that over the past year and a half the economy had successfully transferred a large amount of productive resources from defense to civilian purposes as well as weathered a major readjustment related primarily to business inventory holdings. Adjustments on both counts seem to have about run their course, he said, as defense outlays have stopped declining and productive activity and final demands are now in a better functional balance.

Mr. Sproul stated that he was in general agreement with the description of recent developments given by Mr. Young and as set out in the staff memorandum, except perhaps for some of the adjectives such as "dramatic". He had in mind the special difficulties of interpreting recent data because of changed seasonal factors, particularly the earlier model changeover in automobiles which accounts for much of the drama. In other fields of industrial production than those connected with automobiles, increases have been relatively modest. If the advanced seasonal is important, Mr. Sproul felt that continued increases in total industrial production at the recent pace would not seem likely, particularly as there is little evidence in current price statistics that there will be a substantial shift to inventory accumulation at this time. The increase in production schedules for automobiles should not be linked too closely to current sales, since some of the present high production might be partly precautionary because of strike possibilities. If such a strike takes place the automobile companies would be in a position to meet demand for cars, but if a strike does not take place current production levels would leave a very large inventory problem. Mr. Sproul also had some doubts about the staying power of the construction boom and some concern about the employment situation in the light of the gap between increased output and employment opportunities that were developing with increased productivity and the rising labor force.

Mr. C. S. Young then made a statement in which he said that industrial activity appears to have scored a sharper advance in the Midwest than in the nation as a whole in recent months, largely due to the spectacular upsurge in new automobile production. This development has affected not only Michigan centers, but also many other district cities where parts plants and materials suppliers are located. The higher rate of automobile output and related activities will continue at least through March, Mr. Young said, since firms have tentatively scheduled output of nearly two million units during the quarter, which is 40 per cent more than in the first quarter of 1954. If this schedule is met and inventories are to be kept in reasonable bounds, dealer sales will have to be at least one-third higher than in early 1954 and ten per cent above the record first quarter volume of 1-1/2 million sales reached in 1951. Even with such a favorable sales experience, inventories would rise from an estimated 400,000 units at the end of December to about 650,000 units at the end of March. Consumer acceptance of new-model automobiles apparently has been very good so far and retail deliveries in December are estimated at about 550,000 units, half again as large as last year and about the same as the December 1950 all-time high. As to other retail lines, Mr. Young commented that while department stores in Chicago did not regard inventories in most lines as unduly low, activity at the recent Chicago Furniture Show was reported to be higher than last year, and a majority of firms reporting to the trade association anticipated an increase in volume averaging 5 per cent for the first half of 1955.

Mr. Young also said that, despite the pickup in the automobile industry, the labor supply is ample in virtually all cities of the Seventh District and unemployment is estimated at about 5 per cent of the entire labor force. It might be that things are not quite as rosy as they appear on the surface and that some of the automobile companies are borrowing from the future in maintaining current production schedules.

Mr. Thomas made a statement with respect to capital market developments, the Treasury's cash position, recent changes in the volume of bank credit, and member bank reserves and money rates. These comments were substantially in accord with those contained in the latter part of the staff memorandum dated January 7, 1955, which had been sent to all members of the Committee before this meeting. In particular, he pointed out that practically all categories of bank loans increased further in December and bank deposits and currency holdings showed a more than seasonal increase. For the year 1954 as a whole total loans and investments of commercial banks showed the largest increase of any postwar year, and demand deposits and currency increased by 3 per cent, with a seasonally adjusted annual rate of increase of nearly 6 per cent in the last half of the year.

Mr. Thomas also presented a sheet containing an estimated pattern of reserve changes, by weeks, during January-April 1955. This showed that, in the absence of Federal Reserve open market operations, daily average free reserves might be expected to increase approximately $250 million during the statement week ending January 12; $410 million during the statement week ending January 19; and $129 million during the statement week ending January 26. The tabulation also indicated that on the basis of these projections, if the volume of free reserves were to be kept from rising above the $300 million level after the week ending January 5, it would be necessary to engage in open market operations (through letting bills mature or making sales) in the amount of about $400 million in each of the weeks ending January 12 and 19, and perhaps in an amount somewhat in excess of $100 million during the week ending January 26.

Chairman Martin then made a statement substantially as follows:

> I would like to explain why we have called the full Open Market Committee together at this time. One of the things that has worried me is that the line between operations and policy gets very thin at times, and the line between what responsibilities the executive committee can legitimately take and the line that shows when it ought to consult the full Committee is a very fine one. Perhaps we ought to have more meetings of the full Committee, particularly when there are changes in the general situation such as we have been having lately. It is perfectly obvious that there are differences among us in the evaluation of the changes, and it is important that we review these changes in the scene as they are taking place.
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> We have talked a lot about "nipping the recovery in the bud". We now have a very happy situation so far as our

economic activity is concerned. What we are wrestling with at the moment is the possibility that inflationary seeds may be germinating, and that when they come to full bloom it will be exceedingly difficult to restrain them. As a Committee, we ought to do everything we can to permit the development of the prosperity we are all seeking. But these words mean different things to all of us. I have looked through some of the records of meetings in the past few years and there obviously have been shades of degree and emphasis in the minds of all of us; that is why all of us should meet from time to time and review the shades of emphasis. I was a little worried because I know the management of the account has been trying faithfully to carry out the directives given it, and it has found it difficult at times to be sure of just what these different shades of emphasis called for in operations. We have talked about $400-700 million of free reserves at times and about resolving doubts on the upside and not on the low side, and we have talked about a lower range of reserves and whether there should be less active ease. I have wondered whether the shifting scene has not taken these figures and terms out of focus, when you talk about "ease" and "active ease" and when you remember that there are these different shades of meaning in our discussions that are not spelled out in our directives. It may be that no change is called for in the directive of the full Committee at this time but at least I felt we should meet to go over the current situation.

My own thinking has been along these lines: the point Mr. Sproul has made about seasonals is a very real one, particularly for the automobile industry. All of us have to realize, however, that when we talk with businessmen when things are going very well, businessmen are inclined not to get too rosy in their comments. Also when they are pessimistic they are apt to be more pessimistic in their comments than they actually feel. I recently talked with the head of a large steel company who is so optimistic that I would not dream of selling stock in his company if I had any. He feels we are going through the roof. I think the figures Mr. Thomas has cited on the money aspects place upon us some responsibility for the conditions of ease that exist in the securities market. We have different views around this table about what action is appropriate in that direction and about what could be done. I want to emphasize that selective controls are never alternatives in my thinking to general controls. They are supplementary, but they are not alternatives.

We have to have a coordinated program and if the blackness that may be in the future (I happen to be on the optimistic side at the moment) is to come, it is all the more important that we use flexible monetary policy during a period when we are not trying to bring the horses to a halt, but to let the horses know that they cannot go off in any direction they want. Never in my experience have I seen a solider, stronger securities market. It is not coming from margin purchases; it is coming from certain shifts in holdings, recapitalizations, and so on. We cannot absolve ourselves from responsibility by saying that we will increase margins another 10 per cent or more. To continue to use in our directive the word "promote" in speaking of ease seems to me to be uncalled for at this time. We ought not to be "promoting" ease now. Granting the seasonal conditions Mr. Sproul has pointed out, and granting the basis for the apprehension Mr. Young has pointed out in speaking of conditions in the Chicago District, I think that the economic future of the country is moving forward rapidly. It seems to me that in place of the word "promote" we ought to substitute the word "foster". We might change the phrase to "fostering growth and stability in the economy" and we might include something about avoiding unsound conditions or inflation. We are in the dilemma of not wanting to "nip recovery in the bud" but we want to "nip inflation in the bud". We want to see that we don't have too much "fluff". I was delighted that General Motors decided to go to the market for equity financing but we want to show in our monetary policy that we are not so wedded to the conditions of ease that we promote a psychology that becomes uncontrollable.

We have a particularly difficult problem with the Treasury's financing. I had some discussions with them at the time the margin requirement change was made. They are considering a long-term bond. We certainly don't want a weak market while they are doing their financing. There is a relatively limited period of time in which we can operate. I think we ought to show, during the time the Treasury is doing its financing, that we are on the constructive side. It is because of the conjunction of all these problems that I feel it is desirable to have the full Committee get together. We need to get the benefit of the thinking of all of you and to consider whether there is anything to my point of substituting the word "fostering" for promoting and of putting something about "avoiding unsound conditions" into the directive to the executive committee. We have been operating under a directive that calls for ease and we have gone as high as $900 million or a billion dollars of free reserves and have said that was active ease. Now I think we have a reverse trend. I don't think we ought to be talking too much about the future. We ought always to be thinking about the present. I don't want to be misled by phraseology. I think Mr. Sproul's point is well taken on the seasonal factor, but that seasonal influence has been with us for a long time and it is now highlighted by the automobile industry in particular. If there is to be a glut in the automobile industry we ought to have some leeway so that we can operate in the opposite direction. I sincerely think we have gotten too far out on the limb of easy money. Our position has been interpreted that there will be an endless stream of reserves, and when you get to the point where an insurance company hocks a large block of its mortgages I think we ought to be extremely watchful about the current situation. It may well be that my judgment is not correct, but I think it important we continue to view these problems. We ought to try to have a coordinated policy. We ought to be considering, if this goes on, tightening the money market, and we ought to be considering the possibility of another signal to the stock market either through a further increase in the margin or, preferably, through the discount rate. We ought to be considering something of a cautionary nature.

I am not going to call on everyone here today. I would like to have Mr. Sproul give us the benefit of his thinking and would like to have whoever feels called upon to do so make whatever contribution he feels would be helpful in our discussion.

Mr. Sproul then made a statement substantially as follows:

1. First, I would like to say that I think the action of the Board of Governors in raising margin requirements last week was a timely and appropriate move, as a warning concerning the use of credit in the stock market, and having in mind the possible effect of movements in the stock market on the whole economy. I also think that it was a proper use of a selective credit control in the sense of supplementing over-all credit policy; it was in accord with the action taken by the Federal Open Market Committee at its last meeting changing the wording of its directive to the executive committee from one calling for the maintenance of active ease in the money markets to one calling for the maintenance of ease.

2. Second, I agree that economic recovery is no longer in the "bud" but I question whether such inflationary pressures as exist now need to be or can be nipped in the bud by general credit controls. We have an economy in which long-term growth factors and cyclical recovery factors are combining to produce a vigorous upturn, which seems likely to persist for some time, and I would not want to see it hindered at this stage by general credit restraints.
3. To discuss this question, in terms of open market policy, it seems to me that we may need to have a clearer understanding of some of the terms we have been using to label open market policy. In our discussions we have gotten into the habit of using such terms as "active ease", "ease", "neutrality", and "restraint", but we seldom try to define what these terms mean. We need also to recognize that they only label broad general policies, and that there can be numerous gradations of policy within broad general policies. Changes are ordinarily made gradually within the limits of a broadly defined policy, not by abrupt movements from one policy to another. That is a difficulty in catching in a phrase, of a directive, these refinements of policy and the thinking of each of twelve individuals which led to those refinements.
4. To assist my own thinking, and as a rough approximation of present meaning I have tried to give some definition to the terms we have been using.

<u>"Active ease"</u>

(a) Maintenance of a volume of excess reserves large enough to assure ready availability of bank credit, in ample volume for all borrowing needs meeting ordinary standards of credit worthiness. This ease should be expected in time to pervade all credit and capital markets.

(b) The discount rate at a low level.

(c) Relatively low interest rates at all maturities, with a tendency toward a continuing decline of rates whether or not continued declines are desired as a matter of policy.

(d) Short-term money market rates ordinarily far enough below the discount rate so that access to reserve funds will be cheaper through the open market than through the discount window.

(e) Member bank borrowing from the Federal Reserve Banks only intermittently, and in small volume by reason of individual bank situations.

"Ease"

(a) Bank reserves and bank credit continue readily available to meet credit-worthy demands; no need of allocation of funds, on part of banking system as a whole, to particular uses because there is not enough credit to go around; but no pressure on the banks to find uses for a continuously increasing supply of reserves.
(b) Discount rate continues at a low level.
(c) Tendency toward decline in other rates of interest (existing during period of "active ease") is checked and some rates advance.
(d) The more sensitive money market rates - Federal funds, dealer loans, and Treasury bills - move up toward discount rate so that, at times, borrowing reserves through discount window may be more advantageous than obtaining them through the open market.
(e) Individual member banks borrow with some frequency in initial response to expanding credit needs but a sustained and growing aggregate volume of borrowing is soon relieved by open market operations.

"Neutrality"

(a) Volume of bank reserves still ample to meet credit-worthy demands. Market factors allowed to express themselves in the reserve position of banks. This would mean, in most instances, no continuous cushion of excess reserves and the elimination of free reserves in the aggregate.
(b) Any appreciable change in economic conditions or over-all credit demands would have a fairly prompt reflection in more sensitive rates of interest and, if there were tightening tendencies, the sensitive money market rates would be expected to move above the discount rate.
(c) At some stage, if these tendencies continue, the discount rate would be moved up toward what might be considered the middle of its range.

(d) A moderate volume of member bank borrowing might be outstanding much of the time, but continuing pressure on the banking system as a whole to meet its needs by heavy borrowing would eventually be resisted by open market operations.

"Restraint"

(a) Through absorption of reserves or reluctance to provide reserves through open market operations, general awareness would be created that bank credit is not available in sufficient volume to meet all of the demands that are being made upon it.

(b) Pressure of an excess aggregate demand of credit upon a limited over-all supply would be expected to cause higher rates of interest, and there may be a tendency for rates to rise whether or not intensification of pressure is desired. (Our experience in early 1953 is an example, perhaps.)

(c) The discount rate would be raised in confirmation of the general policy of restraint, to the higher levels of its range.

(d) Sensitive money market rates would be close to or above the discount rate at all times.

(e) A substantial growth of member bank borrowing should take place, as a result of excess credit demands, which would only be moderated by open market operations if the apparent degree of restraint was becoming too great.

(f) Reserves continue available at all times at a price - the objective is not to shut off bank credit or even a net reduction, but to limit growth so as to avoid inflationary pressures from the monetary side.

5. In these terms, the present economic situation still seems to me to call for a policy of "ease", call it minimum ease if you want, rather than a neutral or restrictive policy. Cyclical recovery from the recession of 1953-54 has shown additional vigor in the last two months and the economy seems likely to continue strong during the next few months. But it still remains true that the revival reflects more a cessation of deflationary influences than the emergence of new and continuing expansionary forces. The most recent dynamic factors in the

recovery - the early date of model change and the upsurge of automobile production, and the continuing stimulus of very liberal credit terms in the home construction industry are not new expansionary forces and may possibly carry the seeds of their own deflation later in the year. With inventory liquidation only now coming to a halt, with nonfarm prices generally stable and farm prices still declining, with high productive capacity facing increased competition, with the possibility of a continuing problem of unemployment and major labor conflicts, and with the Treasury taking funds out of the economy instead of putting them in as during the past six months, there seem to me to be economic (and political) dangers in trying to reach, by general credit measures of a more restrictive nature, whatever spots of speculation or inflation may seem to be developing at the moment.

6. So far as credit policy is concerned, it should be emphasized that right now we want to meet the credit requirements of cyclical recovery as well as secular growth. Without creating a general inflationary bias or the need for a neutral or restrictive credit policy, this combination of demands might lead to a less than "seasonal" decline in the use of bank credit during the first half of 1955, or might even result in some desirable expansion of such credit. We should not be led, therefore, by shaky figures of "normal, seasonal" declines in the use of credit to adopt a more restrictive policy than the economic situation justifies.

7. With a continued policy of "ease":
   (a) I would expect banks, and particularly money market banks, to be in a well-balanced position - no longer under pressure, as they were last year, to seek new investments continuously in order to avoid carrying excess reserves, but still ready and eager to meet legitimate loan demands.
   (b) I would expect sensitive short-term money market rates to fluctuate only a little way below the discount rate most of the time.
   (c) And I would expect the discount window to become more of a factor in providing bank reserves.

   This would seem to me to be a healthy situation.

8. Just where free reserves fit into this picture is hard to pinpoint. We have to remember that we are in the process of weaning the banking system from a condition of active ease, and that we want to put on the brakes gradually, and maybe even take them off from time to time. We also have to remember that the distribution of reserves is a variable which can

> be important. So far as free reserves can be used as a guide, therefore, I think we shall have to feel our way down. We may find that over a period of several weeks we can and should get rid of the idea of free reserves, and of free reserves themselves, but I still want to move gradually rather than abruptly at this stage of our economic recovery. A change in the directive of the Federal Open Market Committee to its executive committee, which would call for credit restraint as contrasted with our present policy of less ease, would seem to me to be a mistake.

Mr. Sproul concluded by remarking that he would not wish to see the intent of the directive changed at this time. As regards Chairman Martin's suggestion, Mr. Sproul said that he had no objection to substituting "foster" for "promote" in the directive so long as the Committee understood that our operations were still aimed at the lower end of a condition of "ease".

Chairman Martin stated that he felt all of the members of the Committee had benefited from Mr. Sproul's comments and that he hoped each of them would read Mr. Sproul's statement on the definition of terms. In his (Chairman Martin's) opinion, one of the biggest problems of the Committee was understanding the terms that were used in describing credit policy and in translating those terms into instructions or directives contained in the minutes of the meetings of the Committee. Chairman Martin went on to say that there obviously was a difference of judgment between Mr. Sproul and himself in connection with the economic situation and the credit policy that should be followed, although he did not think it very large. He said that he regretted very much the "leak" that developed in the policy of the Committee immediately following its meeting on December 7, 1954 when the word "actively" was removed from the full Committee's directive to the executive committee in describing the program to be followed in maintaining ease in the market. However, it is necessary to put into the annual record of policy actions of the Federal Open Market Committee a statement with respect to the policy decisions reached at at least four meetings a year—in fact, Chairman Martin said, there was a likelihood that a bill would be introduced in the Congress to require a statement of open market policy decisions each quarter of the year. It was Chairman Martin's view that the Committee should issue its directives in terms that followed as closely as possible the views and words on which there was a meeting of the minds of the members of the Committee. This was difficult but every effort should be made to follow such a procedure. His own personal view as to the current situation was that the use of the word "promote" in the Committee's directive was not appropriate under present circumstances. Chairman Martin said that he was not talking about apprehensions as to the future: that what might happen in the future was partly dependent on what the Committee did in the present. While he did not wish to stress the word "inflation" it was Chairman Martin's judgment that the forces of easy money in the market had gotten out of proportion to what the Committee has been trying to do in the way of promoting growth and stability in the economy. This did not mean that he felt the Committee should go to a policy of restraint but it did involve the problem of the exact meaning of such words as "ease", "active ease", "neutrality", and "restraint". While there had been a time when he felt "neutrality" was quite an important word, Chairman Martin said he was not sure of its meaning. He was sure, however, that the psychological reaction of the market was different at different times. He was convinced that the Committee recently had been operating with much too high a level of reserves and that, whatever the words used to indicate a change, flexible monetary policy called for a recognition of this situation. If the Committee after discussion did not feel that any change should be made in the directive, then the directive should remain unchanged. But it was important to make the directive reflect whatever the Committee felt fitted the situation at a given time. Chairman Martin did not think that he and Mr. Sproul were far apart on the level of free reserves that would be desirable but if open market operations were to be such that there would be "zero" free reserves for a time, he would prefer as a member of the executive committee that the directive from the full Committee be changed at this meeting to recognize a shift in emphasis.

Mr. Mills said that he would like to express a midpoint view. He thought the Committee was thinking of a "firm" money policy, not a policy of tightness or of ease. While he did not have the concern regarding the wording of the directive that had been expressed earlier in the meeting, he said that he was concerned as to how the directive of the Committee would be interpreted by the management of the account as it carried out operations under the continuing directives of the executive committee. Mr. Mills felt the present period was one of economic flux which deserved a cautious approach to future policy. The Committee had moved from its policy of active ease to a climate of "firmness". While the Committee wished to slow down investment activities, as in the long-term mortgage field, it would wish, if possible, to avoid choking off legitimate activities. Mr. Mills felt that whatever directive was decided upon, it would be desirable to vest the executive committee with an authority which would avoid a too rigid interpretation of the instruction: the instruction should be flexible enough to permit, if the executive committee found it was moving too severely toward a situation of tightness, relaxing from that position without need for going back to the full Committee.

Chairman Martin said that Mr. Mills had made an excellent contribution to the discussion, that it was particularly appropriate in view of the Treasury's position. Also, he noted that Mr. Mills had added the word "firmness" to the group of words Mr. Sproul had commented on in his statement. It was these different shades of meaning and emphasis that should be thought through, he said, in terms of the objectives of the Open Market Committee and the contribution that monetary policy could make under any given conditions.

Mr. Leedy felt that continuation of the word "ease" in the full Committee's directive might subject the Committee later on to an appraisal which it would not desire. It was evident, he said, that there were some excesses in the present situation, as in the securities market, and it was his view that at this juncture the Committee's record should indicate a directive to the executive committee to be moving in the direction of firmness, rather than to be continuing with wording that had gotten into the directive at a time the Committee was actively promoting ease. Mr. Leedy suggested that clause (a) of the full Committee's directive might well be amended by adding to it words which would make it read that open market operations should be with a view "to relating the supply of funds in the market to the needs of commerce and business by effecting an orderly reduction in the monetary supply responsive to seasonal requirements." He also suggested that clause (b) be changed so that the Committee's directive would not call for "promoting" or even "maintaining" a condition of ease. He questioned whether a program of operations such as Mr. Sproul had outlined could be carried out under the existing directive without violating the ordinary meaning of its terms.

Mr. Robertson, after stating why he felt it desirable to have meetings of the full Committee as frequently as might be called for because of differences of opinion, said that while he did not think the Committee was fighting inflation today, it was trying to prevent development of inflation. With that in mind and with the thought of a progression from a state of "active ease" to "ease" to something else, he would suggest that clause (b) of the Committee's directive be changed to indicate that open market operations should be with a view "to promoting long-term growth and stability in the economy by maintaining for the time being a condition of mild restraint." He did not care so much what the precise wording of the directive was and would have no objection to the wording Chairman Martin had suggested indicating that the Committee wished to avoid unsound conditions, but he did feel that the directive should show that the Committee was now moving from a condition of ease to something like mild restraint.

Mr. Williams stated that for purposes of perspective he would like to approach the problem of credit policy from another angle. During the past week, he said, he had been in touch with five individuals who had complained about the unusual competition that existed in business and about the pressures that existed on prices. He also cited complaints of automobile dealers that manufacturers were failing to protect dealers' territories. In another instance, the head of a large corporation had caused a survey to be started in his plant with a view to effecting all possible economies. Mr. Williams also stated that real estate firms had expressed concern about recent tendencies in credit policy and that one member of the Philadelphia Bank's Board had predicted that later this year there would be considerable weakness in the market for older houses, so much so that the advantages of going into an old house would be so great that many persons would turn from purchases of new houses which could be bought with no down payment and would instead purchase the older houses. Mr. Williams thought these factors added up to saying that the spirit of optimism which seemed so unanimous might grow out of special factors, rather than influences that were generally present in the economy. He could see nothing to indicate an incipient boom, and he did not think the Committee should go on record by inserting the words "mild restraint" in its directive. He would accept "fostering" in place of "promoting" and he would be agreeable to inserting a phrase that would suggest the avoidance of unsound conditions, but he did not think the existing policy of the Committee should be changed very much. While he would be willing to see the Committee working down a little in the amount of ease, it should not actually work in the other direction, that is, in the direction of restraint. In response to Chairman Martin's question, Mr. Williams agreed that what he was suggesting was working a little further toward the middle-ground in credit policy.

Mr. Balderston said he thought the recovery taking place was one which needed to be sustained and that this required attention to two incipient trends: (a) impairment of the quality of mortgage debt and automobile instalment paper, and (b) the climate of speculative activity that stemmed from conditions in the market. This led him to favor some change in the wording of the directive, preferably along the lines Chairman Martin suggested. More importantly, Mr. Balderston said, he would favor a change in target to a zero amount of free reserves and bill rates approximating or perhaps exceeding the present discount rate. Mr. Balderston said he was thinking of the problem that would face the System in the future of perhaps making an adjustment in the discount rate—he wished it were now 1-1/4 per cent instead of the existing 1-1/2 per cent rate.

Chairman Martin then summarized the several suggestions made, namely, Mr. Leedy's suggestion for a change in clause (a) of the directive which would call for effecting an orderly reduction in the monetary supply responsive to seasonal requirements; his own suggestion which would call for a change in clause (b) of the directive so as to provide for the conduct of operations with a view to "fostering" (rather than "promoting") growth and stability in the economy and avoiding the development of unsound conditions; Mr. Robertson's suggestion which would include insertion in the directive of "long-term" before "growth snd stability" and of words indicating that the Committee was moving from a policy of ease to one of mild restraint; and Mr. Williams' caveat that whatever the change, the Committee avoid any wording of its directive which would indicate it was moving to a policy of mild restraint.

In a brief discussion of Mr. Robertson's suggestion that "long-term" be inserted before "growth and stability", it was the consensus that the idea of long-term was inherent in the objective of promoting or fostering growth and stability in the economy and, accordingly, that the addition of the words "long-term" was unnecessary. Mr. Thomas commented that the use of the words "growth and stability" as a part of the Committee's directive implied a sustained growth but that growth could not be sustained if it proceeded too fast.

Mr. Szymczak suggested that regardless of the wording chosen for the directive, the important thing was to discuss the policy which the Committee wished to follow to see if there could be a meeting of minds as to what the Committee meant when it used different terms. This would help when the executive committee and the Manager of the System Account came to interpreting directives given to them.

Chairman Martin stated that he felt the framework of what the Committee was trying to do at this time was fairly clear, but he doubted whether agreement could be reached at this meeting on definitions of terms.

Mr. Szymczak responded that he felt a study of the suggestions made by Mr. Sproul and of the changes proposed in the directive by Messrs. Leedy and Robertson would help in the future.

Mr. Earhart suggested that the Committee at least take the word "ease" out of its directive at this time. He could see no harm in taking it out and felt it would make a better record since it appeared the Committee did not now wish to be "pushing" reserves into the market.

In the course of further discussion, Mr. Robertson suggested that in place of the words "mild restraint" which he had suggested earlier it might be preferable to use the term Mr. Mills had used—"firmness"—as indicating the kind of policy the Committee had in mind.

Mr. Sproul stated that he did not think the wording of the directive made too much difference if there was general agreement on what the Committee proposed to do and if the Committee knew what the executive committee was expected to do. With gross national product still $5 billion below what it was in mid-1953 and thinking in terms of an economy that would grow over the long term, Mr. Sproul could see no basis now for introducing the word "firmness" into the Committee's directive. This would indicate a policy of restraint, and he felt the economy was still in that part of the quadrant of a circle calling for ease but working gradually toward the next step. However, so long as there was understanding as to the meaning of the words used and so long as the Committee understood that it was gradually feeling its way and not adopting a policy of restraint, he would not be concerned about the wording of the directive although he would prefer that it not be changed.

Chairman Martin then read a statement which Mr. Riefler had prepared indicating that the various views expressed all amounted to saying that the Committee wanted credit policy to be carried out with a view "to fostering growth and stability in the economy by effecting for the present an orderly reduction in the supply of free reserves."

Mr. Rouse said that this was about the conclusion he had come to: that the Committee had in mind gradually contracting the volume of free reserves from its present level.

No disagreement was indicated with the statements of Messrs. Riefler and Rouse as reflecting what the Committee had in mind as to policy for the immediate future, but Mr. Szymczak thought it would not be desirable to inject the words "free reserves" into the directive.

There was a further discussion of the several suggestions made for change in the wording of the directive and of the desirability of having wording which applied to the immediate situation, rather than a statement of a general objective of credit policy good for all time to come. In the course of this discussion, Mr. Szymczak again suggested that it might be desirable to make a further study of the suggestions made by Mr. Sproul as to the definitions of terms; in the meantime, without changing the directive of the full Committee, the executive committee could work within the framework of a policy along the lines discussed at this meeting.

Chairman Martin responded that if the Committee was going to act now to authorize a policy along the lines of the discussion, he felt the Committee should agree at this meeting on a phrase which was representative of the shade of opinion on which there was agreement at the meeting today.

Mr. Irons then suggested that while he was not a member or alternate member of the Committee, the tenor of the discussion indicated to him that clause (b) of the Committee's directive would be given a meaningful wording if it were to provide that operations should be with a view "to promoting growth and stability in the economy by maintaining conditions in the money market so as to avoid the development of unsustainable expansion".

After discussion of Mr. Irons' suggestion, Mr. Sproul moved that the Committee modify clause (b) of the first paragraph of its directive to the executive committee to read, "to fostering growth and stability in the economy by maintaining conditions in the money market that would encourage recovery and avoid the development of unsustainable expansion".

Mr. Sproul's motion was put by the Chair and carried. On this motion, Mr. Bryan requested that he be recorded as "not voting". In connection with his request that he be recorded as not voting, Mr. Bryan made a statement substantially as follows:

I should like to be recorded as not voting. This request is made because I came to this meeting prepared to discuss the economic situation, and prepared to discuss appropriate policy in terms of reserves and money rates. I find myself ill-prepared to discuss textual changes in the directive of the

Committee, and least of all prepared, in the light of the discussion we have had to appraise the significance of the textual changes actually adopted, or the magnitude of the policy changes contemplated by the changes of language. In view of this lack of preparation and understanding on my part, I believe that it is wisest for me not to vote either for or against the proposal.

It seems to me that there is a difference of opinion, or a substantial difference of emphasis, as to what our actual policy should be in the light of current economic events. We have not, I believe, come to grips with that fundamental and basic difference of opinion in terms of free reserves, total reserves, or money rates but have devoted ourselves to a textual change in the directive that conceals rather than reveals our differences. That textual change is apparently intended to signal a change of policy but not in a way that makes reasonably clear to the executive committee and the agent for the account what actual policy is intended. Please forgive the opinion that we have attained a semantic solution that does not set forth what it is that we want to do, and does not clearly enough tell our agent committee and agent bank what we have in mind.

If I were the agent bank, or the agent executive committee, charged with the responsibility of effecting the intentions of the full Committee, I would be fearful of so vague a directive. I would have no way of certainly proving that I had discharged my responsibilities and would thus court the danger of being second-guessed and falsely suspected, which is a human tendency in any event and almost inevitable when the principal is a committee and the agent is given a directive that conceals differences of opinion regarding the proper policy, or the proper extent of policy change, or both.

An important source of our difficulty in writing a directive, and an important source of danger to the agent executive committee and agent bank, I believe, is that we have been trying to use terms that are qualitative in nature. Qualitative terms have great use in certain fields, but I doubt if they are of much help to any of us here in saying what we want to do, unless, as Mr. Sproul has commendably attempted, we define those terms with considerable precision. Unfortunately, qualitative terms run into the difficulty that they must usually be defined by other terms that are qualitative in nature. Thus, we have many terms such as ease, active ease, firmness, restraint, mild restraint, and so on. It may be that these terms can be sufficiently defined that there is a minimal room for difference of opinion as to the policy intended, the authority delegated, and the discharge of the delegation; but I am now tempted to the opinion that we will understand our policy better, and make a better discharge of our responsibilities, within acceptable canons of delegation as between principal and agent, the more nearly we develop directives that avoid qualitative terms and approach directives in quantitative terms, whether free reserves, total reserves, money rates, or money-rate ranges.

On the economic situation, I share totally the views expressed by Mr. Sproul and Mr. Williams. I quarrel with nobody's conjectures, but it seems to me that we have the problem of taking up slack in the economy and of providing for a growth sufficient to provide for a rapidly expanding working population. I cannot see, by an examination of prices or employment levels, any real inflationary problem at this time. Therefore, I am extremely concerned, as I was in December, when I reluctantly voted to take the word "active" out of the policy directive as describing our policy of monetary ease, that any actual change in policy—whatever words we may use in the directive—be very tentative, very hesitant, very experimental, lest we send a pall over the economy.

In response to Chairman Martin's question as to the limitation to be included in the directive to be issued to the executive committee, Mr. Rouse stated that he felt the existing limitation of $2 billion in each paragraph was satisfactory.

Thereupon, upon motion duly made and seconded, the following directive to the executive committee was approved, Mr. Bryan not voting for the reasons indicated above:

The executive committee is directed, until otherwise directed by the Federal Open Market Committee, to arrange for such transactions for the System open market account, either in the open market or directly with the Treasury (including purchases, sales, exchanges, replacement of maturing securities, and letting maturities run off without replacement), as may be necessary, in the light of current and prospective economic conditions and the general credit situation of the country, with a view (a) to relating the supply of funds in the market to the needs of commerce and business, (b) to fostering growth and stability in the economy by maintaining conditions in the money market that would encourage recovery and avoid the development of unsustainable expansion, (c) to correcting a disorderly situation in the Government securities market, and (d) to the practical administration of the account; provided that the aggregate amount of securities held in the System account (including commitments for the purchase or sale of securities for the account) at the close of this date, other than special short-term certificates of indebtedness purchased from time to time for the temporary accommodation of the Treasury, shall not be increased or decreased by more than $2,000,000,000.

The executive committee is further directed, until otherwise directed by the Federal Open Market Committee, to arrange for the purchase direct from the Treasury for the account of the Federal Reserve Bank of New York (which Bank shall have discretion, in cases where it seems desirable, to issue participations to one or more Federal Reserve Banks) of such amounts of special short-term certificates of indebtedness as may be necessary from time to time for the temporary accommodation of the Treasury, provided that the total amount of such certificates held at any one time by the Federal Reserve Banks shall not exceed in the aggregate $2,000,000,000.

It was agreed that the next meeting of the Committee would be held during the week beginning February 28, 1955.

Thereupon the meeting adjourned.

Winfield W. Riefler

Secretary