A meeting of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System in Washington on Tuesday, March 7, 1961, at 10:00 a.m.

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

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

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

Mr. Young, Secretary
Mr. Sherman, Assistant Secretary
Mr. Kenyon, Assistant Secretary
Mr. Hackley, General Counsel
Mr. Hexter, Assistant General Counsel
Mr. Thomas, Economist
Messrs. Einzig, Garvy, Mitchell, Noyes and Walker, Associate Economists
Mr. Rouse, Manager, System Open Market Account

Mr. Molony, Assistant to the Board of Governors
Mr. Marget, Director, Division of International Finance
Messrs. Holland and Koch, Advisers, Division of Research and Statistics, Board of Governors
Mr. Knipe, Consultant to the Chairman, Board of Governors
Mr. Yager, Economist, Government Finance Section, Division of Research and Statistics, Board of Governors

Mr. Petersen, Special Assistant, Office of the Secretary, Board of Governors
Messrs. Eastburn, Jones, Parsons, and Tow, Vice Presidents of the Federal Reserve Banks of Philadelphia, St. Louis, Minneapolis, and Kansas City, respectively
Mr. Black, Assistant Vice President, Federal Reserve Bank of Richmond
Mr. Eisenmenger, Acting Director of Research, Federal Reserve Bank of Boston
Mr. Brandt, Assistant Cashier, Federal Reserve Bank of Atlanta
Mr. Holmes, Manager, Securities Department, Federal Reserve Bank of New York

In the agenda for this meeting, the Secretary reported that advice had been received of the election by the Federal Reserve Banks of members and alternate members of the Federal Open Market Committee for a period of one year commencing March 1, 1961, and that it appeared the persons would be legally qualified to serve after they had executed their oaths of office. Prior to the meeting, each newly elected member and alternate member had executed the required oath of office. The members and alternate members were as follows:

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

Edward A. Wayne, President of the Federal Reserve Bank of Richmond, with George H. Ellis, President of the Federal Reserve Bank of Boston, as alternate member;

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

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

Eliot J. Swan, President of the Federal Reserve Bank of San Francisco, with Frederick L. Deming, President of the Federal Reserve Bank of Minneapolis, as alternate member.

Upon motion duly made and seconded, and by unanimous vote, the following officers of the Federal Open Market Committee were elected to serve until the election of their successors at the first meeting of the Committee after February 28, 1962, with the understanding that in the event of the discontinuance of their official connection with the Board of Governors or with a Federal Reserve Bank, as the case might be, they would cease to have any official connection with the Federal Open Market Committee:

Wm. McC. Martin, Jr.	Chairman
Alfred Hayes	Vice Chairman
Ralph A. Young	Secretary
Merritt Sherman	Assistant Secretary
Kenneth A. Kenyon	Assistant Secretary
Howard H. Hackley	General Counsel
David B. Hexter	Assistant General Counsel
Woodlief Thomas	Economist
Robert S. Einzig, George Garvy, George Mitchell, Guy E. Noyes, Benjamin U. Ratchford, and Charls E. Walker	Associate Economists

Upon motion duly made and seconded, and by unanimous vote, the Federal Reserve Bank of New York was selected to execute transactions for the System Open Market Account until the adjournment of the first meeting of the Committee after February 28, 1962.

Upon motion duly made and seconded, and by unanimous vote, the selection by the Board of Directors of the Federal Reserve Bank of New York of Robert G. Rouse as Manager of the System Open Market Account was approved.

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meetings of the Federal Open Market Committee held on January 24 and February 7, 1961, were approved.

The next item listed on the agenda for consideration was the review of the Committee's continuing operating policies, as follows:

a. It is not now the policy of the Committee to support any pattern of prices and yields in the Government securities market, and intervention in the Government securities market is solely to effectuate the objectives of monetary and credit policy (including correction of disorderly markets).
b. Operations for the System Account in the open market, other than repurchase agreements, shall be confined to short-term securities (except in the correction of disorderly markets), and during a period of Treasury financing there shall be no purchases of (1) maturing issues for which an exchange is being offered, (2) when-issued securities, or (3) outstanding issues of comparable maturities to those being offered for exchange; these policies to be followed until such time as they may be superseded or modified by further action of the Federal Open Market Committee.
c. Transactions for the System Account in the open market shall be entered into solely for the purpose of providing or absorbing reserves (except in the correction of disorderly markets), and shall not include offsetting purchases and sales of securities for the purpose of altering the maturity pattern of the System's portfolio; such policy to be followed until such time as it may be superseded or modified by further action of the Federal Open Market Committee.

Chairman Martin stated that the Ad Hoc Subcommittee appointed at the meeting of the Open Market Committee on January 10, 1961, met yesterday afternoon and had a general discussion. It was the unanimous feeling of the Subcommittee that a great deal of conscientious and excellent work had been done on the study of the continuing operating policies. However, since this was such an important matter, it was felt that it would not be wise to try to hasten to a conclusion. Therefore, it was the suggestion of the Subcommittee that consideration of possible changes in the operating policy statements be tabled in order that everyone might have an opportunity to review and study carefully all of the material compiled by the Subcommittee.

The Chairman then turned to Mr. Young, who stated that in preparation for a recommendation by the Subcommittee on the operating policies the secretariat undertook a draft that was thought to be consistent with the prevailing thinking. This draft was sent to the members of the Subcommittee prior to the meeting yesterday afternoon. Also, after consultation with Chairman Martin, the draft was sent to all Committee members and Presidents not currently serving on the Committee in order to obtain comments and reaction. Various comments and memoranda were received in reply, following which the secretariat took an inventory of the suggestions and recast the original draft material. In doing so, an effort was made to take into account to the fullest extent possible the suggestions that had been advanced, if not directly then by some manner of rephrasing. One issue that remained for decision was whether any revised statements should be called operating "policies" or operating "rules of practice." Another issue was whether the material should be reduced to the fewest possible statements or whether the material should be kept rather inclusive. The New York Bank, for example, had proposed in a memorandum from Mr. Hayes dated March 1, 1961, that the number of rules be kept to a minimum. A further question was whether the authority to engage in transactions in longer-term Government securities should be reserved to the Committee or whether open authority should be given to the Management of the Open Market Account. This question, on which the secretariat went one way and the memorandum from Mr. Hayes went in the other direction, must be thought through carefully by the Committee and a decision reached. There was also the question whether it would be desirable that the Committee's directive to the New York Bank, as the Reserve Bank selected to execute transactions for the System Account, be divided into a standing authorization and a current policy directive. The standing authorization would contain the detailed instructions for operation of the System Account that change only rarely, while the current policy directive would outline the specific monetary objectives to be sought in open market transactions during the period from the close of the meeting at which the directive was adopted until the next meeting. The secretariat rather leaned toward the view that it would be desirable to break the directive into these two parts, and generally that view seemed to have found favor with the Committee members and other Presidents. However, at least one member of the Subcommittee felt that in making the division the Committee should go further and provide a current policy directive that would include enough specifications to define quite precisely the range within which the Manager of the Account might operate until the succeeding meeting of the Committee. This again was a matter that the Committee must think through, discuss, and decide.

Chairman Martin stated that all of the members of the Committee and Presidents not currently serving on the Committee either had or would receive all of the draft material mentioned by Mr. Young. He then said that unless there were general comments this morning, he would suggest that further consideration of the subject be tabled until a later meeting.

Mr. Mills said that on reading the secretariat's proposal and the suggested amendments to it, his reaction had been that the operating policies should be streamlined and that the flexibility in the operation of the Account should be focused in the directive given by the Committee at each of its meetings. He did not know whether other members of the Ad Hoc Subcommittee had approached the problem in that way. However, it seemed to him that this was a fundamental question that must come up for decision by the entire Committee.

The Chairman then turned to Mr. Irons, who said that he thought Mr. Young had presented the issues quite clearly. It would be desirable for all of the Committee members to review fully what had been done thus far, and then the Committee must try to reach a decision.

Chairman Martin pointed out that Mr. Bryan was one of the Committee members originally named to the Ad Hoc Subcommittee. In Mr. Bryan's subsequent absence, his alternate on the Open Market Committee (Mr. Irons) had been asked to participate in the work of the Subcommittee. Now that Mr. Bryan had returned, both he and Mr. Irons would be included on the Subcommittee.

Mr. Hayes said he had a good deal of sympathy with what Mr. Mills had said. It seemed to him that the memorandum he (Mr. Hayes) had submitted spoke for itself. In brief, he felt that the broader and more flexible the statement of operating policies could be, the better it would be in the light of all the present circumstances. There was no disposition at all on his part or, he felt sure, on the part of Mr. Rouse to limit the complete authority of the Committee to change its mind at each meeting and give whatever instructions it desired to the Manager of the Account. However, the idea of having the briefest possible continuing policy statement seemed worthy of consideration.

Mr. Balderston commented that a rather specific current operating directive such as had been suggested by Mr. Irons would be difficult to prepare immediately at the conclusion of each meeting. He (Mr. Balderston) had sympathy with the need for better communication with the Desk by some means. However, if Mr. Irons' idea were favored, thought would have to be given to the method of implementing it.

There being no further comments, it was agreed to table the consideration of the possible changes in the operating policy statements.

Consideration was next given to the continuing authorizations of the Committee customarily reviewed at the first meeting in March of each year, and the actions set forth subsequently in these minutes were taken concerning the matters that had been listed on the agenda for review at this meeting.

> It was agreed unanimously that no action should be taken at this time to amend or terminate the resolution of November 20, 1936, authorizing each Federal Reserve Bank to purchase and sell, at home and abroad, cable transfers, bills of exchange, and bankers' acceptances payable in foreign currencies, to the extent that such purchases and sales may be deemed to be necessary or advisable in connection with the establishment, maintenance, operation, increase, reduction, or discontinuance of accounts of Federal Reserve Banks in foreign countries.

A plan for allocation of securities in the System Open Market Account on the basis of total assets of the Reserve Banks became effective September 1, 1953, pursuant to action of the Federal Open Market Committee at its meeting on June 11, 1953. This procedure was amended at the meeting on March 1, 1960, effective April 1, 1960. Prior to this meeting, there had been distributed to the members of the Committee (1) a memorandum from Messrs. Rouse, Manager of the System Open Market Account, and Farrell, Director of the Board's Division of Bank Operations, dated February 24, 1961, containing a pro forma reallocation of securities held in the System Account as of February 1, 1961, and (2) a memorandum from Messrs. Rouse and Farrell dated February 28, 1961, recommending an amendment to the statement of procedure for allocating the System Open Market Account.

The proposed change in the statement of procedure involved the fourth paragraph only, which currently read as follows:

> 4. Increases and decreases in total amount held in the Account shall be apportioned on the basis of the ratios computed for the latest general reallocation.

Mr. Rouse said that the proposed change, as follows, was intended to clarify the existing language and did not involve any revision of current procedure:

> 4. The Account shall be apportioned during the ensuing twelve months on the basis of the total assets ratios computed for the latest general reallocation after allowing for any adjustments as provided for in Paragraph 3, unless there shall be further adjustments described in Paragraphs 5 or 6.

Thereupon, upon motion duly made and seconded, the procedure for allocation of securities in the System Open Market Account adopted pursuant to action of the Federal Open Market Committee on June 11, 1953, and amended at the meeting on March 1, 1960, effective as of the April 1, 1960, reallocation, was further amended, effective as of the April 3, 1961, reallocation, to reflect incorporation of the change recommended in the memorandum from Messrs. Rouse and Farrell dated February 28, 1961, it being understood that the reallocation to be made as of April 3, 1961, would be based on the ratios of each Reserve Bank's daily average of total assets to the total for all Reserve Banks for the period March 1, 1960, through February 28, 1961.

It was agreed unanimously to continue the existing authorization for distribution of periodic reports prepared by the Federal Reserve Bank of New York for the Federal Open Market Committee, as follows:

1. The Members of the Board of Governors.
2. The Presidents of the twelve Federal Reserve Banks.
3. Officers of the Federal Open Market Committee.

*4. The Secretary of the Treasury.
*5. The Under Secretary of the Treasury for Monetary Affairs.
*6. The Assistant to the Secretary of the Treasury working on debt management problems.
*7. The Fiscal Assistant Secretary of the Treasury.

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* Weekly reports of open market operations only.

8. The Director of the Division of Bank Operations of the Board of Governors.
9. The officer in charge of research at each of the Federal Reserve Banks not represented by its President on the Federal Open Market Committee.
10. The alternate member of the Federal Open Market Committee from the Federal Reserve Bank of New York; the Assistant Vice President of the Federal Reserve Bank of New York working under the Manager of the System Account; the Managers of the Securities Department of the New York Bank; the officer in charge and the Assistant Vice President of the Research Department of the New York Bank; and the confidential files of the New York Bank as the Bank selected to execute transactions for the Federal Open Market Committee.
11. With the approval of a member of the Federal Open Market Committee or any other President of a Federal Reserve Bank, with notice to the Secretary, any other employee of the Board of Governors or of a Federal Reserve Bank.

Unanimous approval was given to the continuation of the authorization to the Manager of the System Account to engage in transactions on a cash as well as a regular delivery basis.

Upon motion duly made and seconded, the Committee approved, with Mr. Robertson dissenting, a renewal of the existing authorization to the Federal Reserve Bank of New York to enter into repurchase agreements with nonbank dealers in United States Government securities, subject to the following conditions:

1. Such agreements
   (a) In no event shall be at a rate below whichever is the lower of (1) the discount rate of the Federal Reserve Bank on eligible commercial paper, or (2) the average issuing rate on the most recent issue of three-month Treasury bills;
   (b) Shall be for periods of not to exceed 15 calendar days;
   (c) Shall cover only Government securities maturing within 15 months; and
   (d) Shall be used as a means of providing the money market with sufficient Federal Reserve funds to avoid undue strain on a day-to-day basis.

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

Mr. Robertson dissented on the ground that in his opinion repurchase agreements are, in fact, not purchases of securities in the open market, such as the Reserve Banks are authorized by law to enter into, but instead are loans to dealers at fixed interest rates that are not related to yield on the securities, and that such loans are beyond the statutory authority of the Reserve Banks. He realized that other members of the Committee considered such purchases legal, but in view of his doubt as to the legality thereof he believed the repurchase agreements should not be entered into on a wholesale basis, as they had been during the past year, but rather should be used only as a last resort to finance dealers who are unable to obtain loans at reasonable rates from others in order to aid them in maintaining an adequate market for Government securities.

Furthermore, he was of the opinion that, for reasons he had stated many times during the past eight years, nonbank dealers should not be given preferential treatment by being furnished loans from the Federal Reserve Bank of New York at lower rates than member banks are obliged to pay for loans from the same Reserve Bank.

The Committee approved, with Mr. Robertson dissenting, a renewal of the authorization to the Federal Reserve Bank of New York (last renewed March 1, 1960) to purchase bankers' acceptances and to enter into repurchase agreements therefor. The authorization was as follows:

The Federal Open Market Committee hereby authorizes the Federal Reserve Bank of New York for its own account to buy from and sell to acceptance dealers and foreign accounts maintained at the Federal Reserve Bank of New York, at market rates of discount, prime bankers' acceptances of the kinds designated in the regulations of the Federal Open Market Committee, at such times and in such amounts as may be advisable and consistent with the general credit policies and instructions of the Federal Open Market Committee, provided that the aggregate amount of such bankers' acceptances held at any one time by the Federal Reserve Bank of New York shall not exceed $75 million, and provided further that such holdings shall not be more than 10 per cent of the total of bankers' acceptances outstanding as shown in the most recent acceptance survey conducted by the Federal Reserve Bank of New York.

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

Mr. Robertson voted against the renewal of the authority to purchase bankers' acceptances because he felt that the Federal Reserve

System should encourage the utmost freedom of market forces and therefore should withdraw from active participation in the acceptance market in the absence of clear indication that such participation would yield specific public interest benefits. He was not aware of any evidence that such benefits had been realized since the authorization was given to the Federal Reserve Bank of New York in 1955. Needless to say, he would oppose the use of repurchase agreements covering bankers' acceptances not only for these reasons but also for the reasons he had given for opposing the use of repurchase agreements covering Government securities.

Mr. Hayes stated that when the acceptance market started in New York the Federal Reserve System took an active interest in promoting and helping it. In his opinion the System had a legitimate interest in doing its part to make that market as broad and sound as possible. Acceptances, he said, are inherently a desirable medium for operations by a central bank. Further, the participation of the Federal Reserve was such a small fraction of the total of acceptances outstanding that in no sense could it be said that the Federal Reserve was making the market.

Mr. Robertson said that he had a fundamental belief in free markets, with as little intervention on the part of Governmental authorities as possible. The acceptance market was an area where it was not necessary to intervene. As he saw it, the Federal Reserve could not help but affect the market through its operations, to no good purpose.

The Committee approved by unanimous vote the continuation without change of the existing authorization for fixing the rate charged on special short-term certificates of indebtedness purchased direct from the Treasury, pursuant to paragraph (2) of the Committee's policy directive to the Federal Reserve Bank of New York, at 1/4 of 1 per cent below the discount rate of the Federal Reserve Bank of New York at the time of such purchase.

The Committee reaffirmed by unanimous vote the authorization for the Chairman to appoint a Federal Reserve Bank to operate the System Account temporarily in case the Federal Reserve Bank of New York is unable to function, such authorization having first been given on March 1, 1951, and having been renewed in March of each year since.

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

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

Such Iterim Committee shall consist of seven members, comprising each regular member and regular alternate of the Federal Open Market Committee then available, together with an additional number, sufficient to make a total of seven, which shall be made up in the following order of priority from those available: (1) each alternate at large (as defined below); (2) each President of a Federal Reserve Bank not then either a regular member or an alternate; (3) each First Vice

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

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

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

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

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

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

(3) Such Federal Reserve Bank may in its discretion purchase special certificates of indebtedness directly from the United States in such amounts as may be needed to cover overdrafts in the general account of the Treasurer of the United States on the books of such Bank or for the temporary accommodation of the Treasury, but such Bank shall take all steps practicable at the time to insure as far as possible that the amount of obligations acquired directly from the United States and held by it, together with the amount of such obligations so acquired and held by all other Federal Reserve Banks, does not exceed $5 billion at any one time.

Authority to take the actions above set forth shall be effective only until such time as the Federal Reserve Bank is able again to establish communications with the Federal Open Market Committee (or the Interim Committee), and such Committee is then functioning.

By unanimous vote, the Committee reaffirmed the authorization given at the meeting on December 16, 1958, and continued at the meeting on March 1, 1960, providing for System personnel assigned to the Office of Civil and Defense Mobilization Classified Location (High Point) on a rotating basis to have access to the resolutions (1) providing for continued operation of the Committee during an emergency and (2) authorizing certain actions by the Federal Reserve Banks during an emergency.

There was unanimous agreement that no action be taken to change the existing procedure, as called for by the resolution adopted June 21, 1939, requesting the Board of Governors to cause its examining force to furnish the Secretary of the Federal Open Market Committee a report of each examination of the System Open Market Account.

Chairman Martin then referred to a memorandum distributed with the agenda under date of March 1, 1961, relating to the procedure authorized at the meeting of March 2, 1955, whereby, in addition to members and officers of the Committee and Reserve Bank Presidents not currently members of the Committee, minutes and other records could be made available to any other employee of the Board of Governors or of a Federal Reserve Bank with the approval of a member of the Committee or other Reserve Bank President, with notice to the Secretary. The most recent list of persons so authorized (exclusive of secretaries and records and duplicating personnel), as shown by the Secretary's records, was attached to the March 1 memorandum.

Chairman Martin asked whether anyone wished to raise a question with respect to the existing procedure, and no questions were heard.

Accordingly, it was agreed unanimously that no action should be taken at this time to amend the procedure authorized on March 2, 1955.

At this point Chairman Martin said that he wished to make the following statement. As indicated by the minutes of the meeting of the Committee on February 7, 1961, it was clearly the understanding that no statement would be released in connection with the decision of the Committee to authorize operations in longer-term Government securities. However, a statement was released on February 20, 1961, coincident with the first operations under the Committee's authorization. He merely wanted to say that although he had cooperated with the Management of the System Account in the issuance of the statement, it was his (Chairman Martin's) decision that the statement should be issued. It was not until the last minute that one could be sure whether or not a statement seemed advisable, but in view of developments that occurred between the date of the Committee meeting and the initial transactions for the System Account, he thought the majority would have supported him in the action taken. At the same time, he did not want anyone to have the impression that the Manager of the Account was in any way acting on his own in making the announcement on February 20; whatever responsibility there was in the matter attached to him (Chairman Martin) and not to the Manager of the Account.

Mr. Rouse said that he would like to share some of the responsibility for issuance of the statement. His thought had been that it was essential to make such a statement if individual dealers, groups of dealers, or other parties were not to have special advantages accruing to them.

Before the meeting there had been distributed to the members of the Committee a report of open market operations covering the period February 7 through March 1, 1961, including a brief review of the period since December 7, 1960. A supplemental report covering the period March 2 through March 6, 1961, had also been distributed. Copies of both reports have been placed in the files of the Committee.

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

> Since the last meeting of the Federal Open Market Committee a month ago, money and reserve conditions have been generally comfortable except immediately before and after the Lincoln day weekend when the situation was aggravated by the sizable cumulative deficit accumulating against the New York banks over the weekend. While we have had some help from unexpectedly high levels of float as a result of bad weather and the airlines strike, the System has been able to add reserves when they were most needed without putting undue downward pressure on short-term rates. Except for the past few days, Treasury bill rates rose over the period, partly because the System found it possible to avoid purchases of Treasury bills by supplying reserves when needed through repurchase agreements and through purchases of other than short-term issues. Here again, the System had some help from (1) the announcement by the large New York banks of their plans for issuing time certificates of deposit to corporations, which would tend to create competition for Treasury bills; (2) the early expectations of a poor bill market until after the March tax date, which now by the way have given way to a more optimistic view; and (3) the growing feeling that the System's new policy of operating in a broader range of issues would mean higher (or at least no lower) short-term rates. Over the past few working days, however, bill rates have again come under downward pressure, and sales of short-term securities have been required to keep this from getting out of hand. The reserve impact of these sales has been more than offset by purchases of other securities. Throughout the period sizable purchases of bills for foreign accounts were kept off the market by selling bills from the System Open Market Account.

It is too early to tell what effect the upward revaluation of the Deutsche mark and the guilder will have on international money flows, and how these flows may affect foreign central bank activity in the Treasury bill market. There was considerable churning in international money markets yesterday. We can only hope that the net result will be to reinforce the recent improvement in the United States balance of payments, but it is becoming increasingly clear that international flows of funds will continue to be of great concern to us, and to monetary authorities abroad, for some time to come.

These and other varied operations all evidenced the high degree of flexibility needed for carrying out the diverse objectives of current open market policy. So far as money conditions and short-term rates are concerned, the System's activities seem to have achieved a fair measure of success without causing undue disruption or confusion in the money and securities markets.

As to the special operations in longer-term issues, we have tried to keep the Committee as fully informed as possible about our operations and the atmosphere in which they have been conducted through the special reports that have been distributed to you. The initial stages of this program have been carried out with reasonable success from the standpoint of market repercussions, which have been remarkably mild so far in view of some of the dire predictions. Dealers responded to the first purchases in a routine manner and appear to have accepted the fact of System operations in longer-term issues as something they can learn to live with. Despite this, there has been, and still remains, a great deal of confusion and misunderstanding which has not yet been dispelled.

At this point what the market needs more than anything is a chance for the furor to die down so that dealers and investors generally can get a better understanding of what the System is trying to accomplish in its operations outside the short-term area. A great deal has been said and written about the operations, much of it misleading and ranging from inaccurate to grossly false. Some progress has been made in encouraging a more moderate attitude in the market, especially among the dealers, but only with time, patient explanation, and further experience can the market arrive at a proper evaluation of the newly created operating conditions.

> The new approach requires a great deal of flexibility at the Desk and we have had to play pretty much by ear, gaining valuable experience as we went along. The lack of dealer position figures for individual dealers has been a real handicap and a request for them has been held in abeyance in the hope that frequency distribution data may prove to be an adequate substitute.
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> Between now and the next meeting of the Committee, it is quite likely that the Treasury will formulate and announce three financing operations: (1) a junior advance refunding, probably from bonds maturing in 1962 into the 6 to 7 year area (It should be pointed out that this operation is still doubtful and should be treated as confidential.); (2) a new cash financing; and (3) a rollover of April 15 bills. Although the publicity over the System's efforts to raise short-term rates and to lower long-term rates might be expected to reduce the advantages of an advance refunding to the holder of the outstanding issues involved, conditions are still reasonably favorable for an operation of this kind and the Treasury has been advised to go ahead with it. If the usual "even keel" is to be maintained during this operation, the System will probably have to face some additional difficulties and dilemmas, particularly in the period surrounding the March 15 tax date when there will be considerable churning in the securities and money markets.

At the instance of Mr. Mills, there was a brief discussion of the prospect of use of the direct borrowing authority by the Treasury around the mid-March tax date, and Messrs. Rouse and Thomas stated reasons why in their opinion it was unlikely that the Treasury would have occasion to resort to that authority.

Mr. Robertson stated that he would like to make certain comments at this point. First, it seemed to him that, despite all the words that had been used, the System had actually engaged over the past few weeks in a pegging operation in respect to the Treasury bill rate, as indicated by the fact that sales were made by the Account yesterday at a time when in his opinion purchases would have been in order. He felt that System operations could not be construed in any way other than an effort to put a floor under the rate on bills. Second, on two occasions during the past few days the Manager of the Account had engaged in swap transactions in the short-term area. Even recognizing the broad authority granted to the Manager by the Committee at the February 7 meeting, Mr. Robertson did not understand that authority for such transactions was included. The minutes contained reference to the swapping of long and short securities, but both of the operations to which he referred involved swaps in the short-term area, which in his opinion went beyond the authority of the Manager except if specifically authorized by the Committee. Third, in his opinion the operations of the Desk during the past period had not been enough in the direction of ease, especially during the past week. He realized that his position favored going further than the Committee consensus, but he did not feel that the operations of the Desk had supplied enough reserves even to be in accord with the consensus.

In reply to a question, Mr. Rouse stated that obviously he would disagree with the comment of Mr. Robertson regarding recent operations, and that he would stand on the reports that had been rendered to the Committee.

Mr. Robertson then inquired whether the Committee had contemplated swap transactions in the short-term area, to which Chairman Martin replied that he had thought that at the February 7 meeting the Committee more or less gave the Account Manager broad authority. The Committee was seeking empirical evidence, and if it was going to obtain that evidence the Desk would have to engage in the necessary transactions.

Mr. King noted that Mr. Robertson had referred to a pegging operation, which term generally carried with it the connotation of inflationary practice. In this instance, however, the effort was to maintain a bill rate higher than might otherwise have developed through market forces. If this was a pegging operation, at least it was for a purpose different than that usually suggested by the use of the term.

Mr. Szymczak commented that current circumstances indicated why it was not feasible for the Committee to attempt to give precise instructions to the Account Management in terms of day-to-day operations. Particularly in view of the diversity of current objectives, the Manager must have latitude to be guided by the feel of the market; he could hardly be expected to operate under detailed instructions. It was not the intent of the Committee to engage in a pegging operation or to do anything except maintain a free market. However, the Committee was attempting to provide reserves to help the domestic economy while at the same time endeavoring to refrain from pushing the short-term rate down because of the problem of the balance of payments.

Mr. Robertson said current operations appeared to constitute an effort to push the short-term rate up, and Mr. Szymczak replied that he thought this was not necessarily the case. Although the short-term rate might go up, the System had no particular level in mind.

Mr. Robertson then commented that the argument, if carried to an extreme, would suggest abolishing the Open Market Committee and authorizing the Manager of the Open Market Account to proceed in his own judgment and discretion.

There followed comments on the statement issued by the Manager, at the Chairman's direction, on February 20, 1961, regarding the extension of System operations into the longer-term area.

Mr. Balderston stated that as one who spoke at the February 7 meeting against the issuance of a statement but who urged extreme care in dealing fairly with all interested parties, he wished to say that his view regarding the issuance of a statement changed completely between February 7 and February 20 in the light of events that transpired. Consequently, he was pleased that the statement was issued. The issuance of the statement avoided the possible criticism that certain parties may have been favored by being given an opportunity not available to others.

Mr. Szymczak stated that he considered the statement appropriately phrased and that he agreed wholeheartedly with the decision to issue it.

Mr. Robertson, who had indicated at the February 7 meeting that he would favor the issuance of a statement if, contrary to his own view, the Committee decided to authorize operations in the longer-term area, stated that he was pleased to observe that members who originally opposed the issuance of a statement had since that time experienced a change of sentiment.

Chairman Martin said he would like to make this observation. He felt sure that it would be better for the System if it could limit its operations to supplying and absorbing reserves and say that its operations had nothing to do with interest rates. However, it was not possible to do that. In talking with critics, he had found it difficult to discuss the question of pegging, which Mr. Robertson had properly brought up, in purist terms. Some people outside the System who were opposed to the idea of pegging nevertheless felt that the System ought to provide some guidance in the market occasionally. The Treasury was issuing quantities of securities from time to time which unquestionably exerted an influence on the rate level. Therefore, while it certainly would be easier for the System if it could say that it was simply going to supply and absorb reserves and have nothing to do with interest rates, the influence exerted by the mere supplying and absorbing of those reserves within the framework of the various factors at work in the market was an influence that must be borne in mind. He did not pretend to know the answer, but he felt it was necessary to keep an open mind. In his view, there was no question but that the activities in which the System was currently engaged could lead to pegging. The Committee should watch developments carefully and study all aspects of the matter.

Thereupon, upon motion duly made and seconded, and by unanimous vote, the open market transactions during the period February 7 through March 6, 1961, were approved, ratified, and confirmed.

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

In the late winter and early spring of 1957, when industrial production and wholesale prices leveled out--while consumer prices and business capital expenditures were continuing to set new records some observers chose to describe the situation as a "tired" or "fading" boom.

The same adjectives might be applied to the recession in the late winter and early spring of 1961. While it is still with us, the downturn seems to have lost momentum.

As the current quarter progresses, there is an increasing probability that gross national product will be down moderately--less than one per cent. In February, industrial production appears to have just about held even--or perhaps declined by one point--we will know in a few days. In any case, it seems unlikely that it will decline further in the current month. The rate of inventory liquidation has leveled and may actually be falling--the book value of manufacturers' inventories declined by only $100 million in January, as compared to a monthly average of $350 million in the fourth quarter. New orders held about even, after several months of decline. Business capital expenditure plans, as reported in the Commerce-SEC survey released yesterday, show a decline of only three per cent for the year, and a small rise from the first to the second half. Recent surveys of consumer confidence and buying intentions have generally been interpreted as optimistic--despite some continued weakness in expressed intentions to buy houses and household durables.

Department store sales have had their ups and downs, as storms this winter have been more frequent and have seemed to hit the weeks that were clear a year ago, but the 147 index for February suggests demand is at least well maintained. The so-called leading indicators produced a strong showing in January, as more than half of them registered gains. Of all the current data, only the continuing lag in automobile sales and the persistence of a high level of unemployment are disturbing. The latter, of course, usually lags as business turns up, and the former is widely attributed to the unusually severe winter in many areas.

I might add here that we have just received the figures on unemployment for February, which are to be released this afternoon. The actual number of persons unemployed rose to 5.7 million, which yields a seasonally adjusted annual rate of 6.8 per cent. This is 0.2 per cent above January, but the same as December. Our technicians feel that the apparent decline in January is attributable to problems of seasonal adjustment and that, in fact, the seasonally adjusted level has remained about the same for the three months.

There are always many good reasons to qualify any appraisal of economic prospects--but there are fewer now than usual. In terms of past experience, almost all the signs point to an increase in economic activity in the coming quarter. Of course, it would be useful to know more, but there is really very little evidence, short of an upturn itself, that one could ask for that is not already at hand, to support the prognosis of a favorable shift in the balance of economic forces.

If one feels that monetary policy should attempt to anticipate changes in business, either for the better or the worse--then the present situation might properly be interpreted as calling for a shift in policy. As I have just suggested, it is unlikely that we shall have any more convincing evidence than we have now that we are approaching a turning point until after the turn has in fact occurred.

Having said this much, I should like to go a little further, to add that it does not seem to me that the situation I have reported calls for any lessening of the degree of ease presently prevailing in credit markets. While some progress has been made there is less liquidity than at the end of other postwar recessions and there is more idle manpower and more idle capacity. The risk of a runaway boom that would take up the slack in the economy and generate serious inflationary pressure quickly seems very small indeed.

The situation in none of the more volatile areas of expenditure--inventory accumulation, business capital outlays, residential construction, or consumer durable goods purchases--seems conducive to the early generation of excessive demands on available resources. Governmental expenditures--Federal, State and local--will undoubtedly increase, but the magnitude of the increase in the months immediately ahead will be moderate. The danger from this source, if a danger in fact develops, will come later.

In brief, developments in the last four weeks appear to confirm, rather than modify, the conclusion presented at the last meeting that we shall see some further decline in the current quarter, followed, in all likelihood, by a gradual recovery.

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

In February short-term interest rates tended to rise, while long-term interest rates declined. Stock prices rose to new high levels on exceptionally active trading. Bank reserve positions were somewhat tighter than they had been in January, although in the latter part of the month the persistence of float at a higher level than usual served to increase free reserves at least temporarily. Total loans and investments of city banks, which declined much less than usual in January, fluctuated rather widely in February, with no pronounced trend. The seasonally adjusted money supply, which increased considerably during January, was at a higher level in February then at any time in over a year, but showed little further growth in the course of the month.

Diverse movements of interest rates in February may no doubt be attributed to some extent to Federal Reserve operations and to the effects on market participants of System and Administration statements as to aims. There were other factors, however, some of which may be transitory. In the short-term area, for example, dealers have considerably reduced their positions in Treasury bills from the large holdings accumulated in December and early January. City bank holdings of bills, which had previously increased, were also reduced in February.

With some reduction in reserve availability in the first half of the month, many member banks needed to borrow in the Federal funds market and occasionally at the Reserve Banks. The discount rate of 3 per cent no doubt serves to prevent much decline in bill rates. Even during the extremely easy reserve periods of 1954 and 1958 the 3-month bill rate generally remained within 3/4 of a percentage point below the discount rate. With similar amounts of free reserves, bill rates were much lower than they are now because the discount rate was lower.

The further decline in long-term rates may be attributed in part to seasonal factors. Yields on long-term bonds by each major issuer group, after declining in the first eight months of last year, rose contra-seasonally from August until December. Declines in these yields from December to the last half of February appear to have been a little less than the usual seasonal decrease. The largest decline occurred in corporate bonds, and this may be due in part to the small volume of new issues in this area. Yields on State and local government bonds have remained relatively firm, reflecting a moderately large volume of new issues and the accumulation of unsold offerings in dealers' inventories.

It may be noted that, contrary to a popular impression, the decline in yields on long-term U.S. Government bonds from the peak reached in January 1960 has been approximately as large as the declines from previous peaks to lows in the two previous recessions. Also, the spread between yields on 3-month Treasury bills and the average yield on long-term Treasury bonds has widened less in the past year than it did in the 1957-58 decline in interest rates. In other words, long-term yields have declined as much as bill yields relative to the previous period of decline.

Total loans and investments at city banks, following a less than seasonal decline in January and a substantial increase in the week of February 1, which was due largely to the special Sears transaction, showed little net change in the four weeks ending March 1 (as indicated by partial data for the latest date). Ordinarily some decline occurs in February. There have been rather wide variations in recent weeks. Increases in loans to business and to sales finance companies during February were roughly in accord with seasonal trends. Loans to dealers in Government securities, which had been rather large in January, declined in February. Holdings of Government securities also declined, but holdings of other securities showed a sizable increase. City bank holdings of Treasury bills were reduced. Reflecting in part the effect of the Treasury refunding operations and the approach to maturity of outstanding issues, the banks' holdings of certificates also declined, but their holdings of notes and bonds maturing within one year increased by almost as much as the decrease in bills and certificates. Holdings of notes and bonds maturing in over a year continued to decline, notwithstanding the shift in the maturity of the new issue.

Demand deposits adjusted at city banks declined by about the usual seasonal amount in February, after declining less than seasonally in January. Time deposits continued to show a greater than seasonal increase. U.S. Government deposits also increased substantially. The daily average, seasonally adjusted money supply continued to increase in the first half of February and preliminary data indicate the possibility of a slightly higher average for the second half of February--the highest level in over a year. Most of the recent increase, however, had already been attained by early February. Weekly data indicate little further growth since that time.

The recent leveling out of monetary growth is reflected in the figures for member bank required reserves relative to projections on the basis of the usual seasonal pattern. After declining substantially less than usual through the week of February 1, changes in required reserves fell below the projected levels during the next three weeks, but then rose, according to preliminary data, in the week of March 1.

Total reserves were maintained in the three weeks ending February 22, in part through a somewhat larger volume of member bank borrowing than had recently been customary, and were kept up in the week of March 1 primarily by the continuation of float at a higher level than expected. All of these differences, however, were too small to be of any great significance. If they have any particular import, it is that there was little or no further monetary expansion after the beginning of February.

In this current statement week and the next, some $500 million of additional reserves will need to be supplied in order to meet current needs and maintain free reserves at close to $600 million. The experience of the last two months indicates that a free reserve level of over $600 million is conducive to credit expansion, while a level below $500 million may not be. Projections of reserve needs around the middle of March are unreliable because of variations in the timing of large tax payments and float. In any event liquidity needs are substantial at that time and reserves should be abundantly available. Substantial amounts will probably be supplied through the midmonth increase in float, and System operations, after supplying reserves in the first half of the month, might be reversed somewhat to absorb some reserves in the last half.

To meet seasonal needs, only moderate increases in the Federal Reserve portfolio will be needed on balance during the second quarter of the year, with the usual intramonth variations. These estimates allow for a continued gold drain of $25 million a week; if this should not develop, System action to supply reserves may need to be negligible except for the intramonth operations. To foster credit growth, however, an additional $50 million or more a month might be needed.

Demands in credit markets in the months ahead might be expected to require more bank reserves than are allowed for in these projections. As indicated in the memorandum on the Treasury cash outlook given to the Committee, even with moderate economic recovery Treasury borrowing needs will be much larger during the remainder of this year than they were last year, and those during the last six months may be as much as $9 or $10 billion, exceeding borrowings in the corresponding periods of 1958 and 1959.

In order to indicate the possible nature and magnitude of demands on the credit system, the Board's staff has made some projections of sources and uses of credit on the basis of stated assumptions as to economic recovery. Net borrowing by State and local governments is likely to increase and to be larger this year than in any previous year. The increase in home mortgages is now running less than in 1959 and 1960 but might be expected to increase in the last half of the year. Corporate borrowing--both at long- and short-term--will probably continue to be smaller than in other recent years.

Total expansion of all types of credit in 1961, under such assumptions, would be similar in amount to 1960 and 1957, but less than in 1955, 1958, and 1959. The commercial banking system will probably be called upon to supply a somewhat larger portion of these credit needs this year than last, principally through additions to holdings of securities, and more than in any other year except 1958. The expansion in bank credit may occur with only a moderate increase in loans. Such expansion in bank credit would be needed to provide for a resumption of expansion in the money supply, which showed little growth in 1959 and 1960. In addition, time deposits at commercial banks will probably continue to increase at close to last year's rate. Consumers may be expected to increase their additions to deposit-type assets, as well as their claims on insurance and pension reserves, but might reduce their holdings of securities. Liquid assets of corporations, which declined last year, might be expected to increase moderately this year in holdings both of cash balances and of Government securities.

This pattern of financial development would call for an increase in bank reserves of well over half a billion dollars in the course of the year--or an average of about $50 million a month in excess of usual seasonal needs. These reserves would need to be supplied by Federal Reserve credit, and any gold outflow would necessitate additional amounts of Federal Reserve credit. Hence, to finance economic recovery the System should supply somewhat more reserves than the usual seasonal needs. If the projected credit demands develop, the availability of reserves in such amounts would not cause a decline in interest rates, but would be needed to prevent too sharp an increase.

In reply to a question by Mr. Mills regarding the weight that should properly be given to seasonal interest rate movements as an element of economic analysis, Mr. Thomas agreed that such data must be studied carefully, that they represented merely a rough indication of the nature of the situation, and that the broad movements over longer periods tended to be more accurate guides.

Mr. Marget then presented the following statement on international financial developments:

> Last Saturday the German government announced an appreciation of the mark. This was closely followed by a comparable announcement by the Netherlands government with respect to the guilder. According to one line of thinking which has become fairly widespread, these actions should be regarded as events of very great importance for the United States balance of payments. For, according to this thinking, the deficit in the United States balance of payments has not only been--as, in a sense, every dificit must be--a reflection of the surplus in the balance of payments of certain other countries, of which Germany was the most notable, but has been the result basically of a wrong set of foreign exchange rates. In particular, the German over-all surplus was alleged to be the result of an undervaluation of the mark. Correct that undervaluation and the German surplus would disappear, and with it the United States deficit, and therefore all the balance-of-payments problems of the United States.
>
> It would be pleasant to believe that the matter is as simple as this. Unfortunately it is not. It might be well, therefore, to review the argument of those who, while they insisted that the decision with respect to the foreign exchange rate of the mark was basically one for the Germans themselves to make, and while they did not regard the prospect of an appreciation of the mark as necessarily portending disaster, nevertheless refused to accept the suggestion that it was in this direction that we must seek salvation of the international payments system in general, and of the United States balance of payments in particular.
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> In the first place, it was known that the extent of the supposed "under-valuation" of the mark, as calculated by those Germans who themselves favored an appreciation of the mark, was very small--around 5 per cent, according to these Germans themselves. And in fact the announced appreciation has been of this order. Given any reasonable degree of flexibility in profit margins, it is difficult to believe that a change of this magnitude will so seriously affect the competitiveness of German industry as to destroy the German surplus at one stroke. On the other hand, it will be interesting to see

what effect the announcement of this small degree of appreciation will have on those movements of capital which have been so largely affected, in recent years, by expectations of an appreciation of the mark. If the speculative fraternity becomes convinced that this is the final answer on the question of the appreciation of the mark, then perhaps we shall have peace in this area for a while, and we may even see some reflow to the United States of funds that went abroad on the expectation of a German appreciation. But if the smallness of the degree of appreciation convinces the speculators that it can be regarded only as a first instalment on a much larger degree of exchange adjustment, it is anything but clear that we shall have the peace that we have been seeking in this field.

It must be said, however, that, if the step was to be taken at all, it was well to take it at this time, when our new Administration's repeated statements of its determination to defend the dollar at its present parity have apparently served to reestablish confidence in our currency. For one of the dangers inherent in an emphasis upon the necessity for an appreciation of the currency of surplus countries is that it encourages an obvious counter-argument that could have very disconcerting consequences: namely, that if it is the exchange rate that is at fault, it is, after all, just as reasonable to insist that the deficit countries correct the situation by depreciating their exchange rates as it is to insist that the surplus countries appreciate theirs.

It may very well happen, indeed, in the days immediately ahead of us, that the very smallness of the degree of appreciation of the mark may lead speculators to precisely this view with respect to the exchange rate of the British pound, and thereby intensify speculative pressure on the pound considerably beyond what was to have been expected in any event as the result of the clear weaknesses in the basic position of sterling, which have until very recently been masked by the very capital movements that have masked the undeniable improvement in the basic balance-of-payments position of the United States. It is to be hoped that this improvement in our basic position, together with the unequivocal commitments of our new Administration, may spare the United States a similar back-lash of speculative sentiment consequent upon the action by the German and Dutch authorities; but on this we shall have to wait and see.

The second reason why some have felt that it was wrong to put all emphasis upon the desirability of appreciating the mark, in particular, as a way of solving the balance-of-payments problems of the United States is really independent of the extent of the appreciation involved. For there is the further issue of the sharing of burdens by the Western alliance: in the fields of development assistance, on the one hand, and a contribution to the joint military effort, on the other. The Germans, to be sure--and, for that matter, a very considerable proportion of the Western financial community, including its central bankers--have persistently denied that there is any connection whatever between a country's balance-of-payments position and its ability to contribute to international efforts in the field of development assistance and joint defense. I cannot take the time here to go over the relevant arguments in detail. But surely one thing is certain: and this is that if a country is to provide a net amount of development assistance, for example, it must have a surplus in its balance of payments. Otherwise there would be nothing to transfer as assistance to the recipient countries. The difficulty with Germany, in this respect, was not that it had a balance-of-payments surplus, a good part of which was going to the less-developed countries; the difficulty was that it had not shown itself willing to finance that surplus, with the result that it acquired a very large amount of monetary reserves from countries which, in one way or another, were financing this development assistance. If, now, the effect of an appreciation of the mark were to destroy the German suprlus, as some commentators have suggested is likely to be the case, we should still be left to face the problem of who is going to provide the development assistance and the means for military expenditures abroad, which certainly makes part of our balance-of-payments problem. It is for this reason that the United States Government, while it has maintained an attitude of neutrality on the subject of the advisability of an appreciation of the mark *per se*, has made it very clear that it does not regard an appreciation of the mark as in any sense a substitute for those measures, in the field of development assistance and military burden-sharing, which it regards as reasonable to expect from Germany as a member of the Western alliance. If Germany does not take the necessary measures in these two fields, the additional burdens will fall upon us; and no amount of sophistication can get around the fact that these additional burdens would seriously aggravate our balance-of-payments problem.

And there is a final, and decisive, reason why it would be extremely unwise to rely for the solution of our own balance-of-payments problem wholly upon the actions of other governments, in the field of exchange-rate policy or in any other field. It is always fair to ask of surplus countries that they follow, in the field of trade and aid, those policies which are characterized collectively as "good creditor policies." But to go beyond this, and to insist, or imply, that nothing can be done by the deficit countries to get their own international accounts in balance and keep them in balance is a position whose inherent absurdity is matched only by its possibilities for a fatal weakening of moral fiber in the field of national policy-making. We have indeed made great progress toward a balancing of our international accounts since the low point of the spring of 1959; and our own policy actions have undoubtedly played a role in the achieving of that progress. If this slight adjustment of the German and Dutch exchange rates turns out, without adverse consequences otherwise, to help along the process of adjustment in our basic position, well and good; but it will still be true that the future of the United States balance of payments, and all that hangs on its, will depend fundamentally upon our own actions: and specifically, and prosaically, on the degree of success we attain in pursuing those policies, in all fields, which will keep us competitive in the markets of the world and here at home.

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

Economic activity has continued to decline moderately, as indicated by January statistics and fragmentary data for February. There is no sign of a speed-up in the recession. On the other hand, although the decline in some series slowed and there was an actual upturn in others, this evidence is too fragmentary to warrant a judgment that the bottom has been reached. Some indications of improvement in February, as in department store and automobile sales, may have been attributable largely to the weather. Consumer buying intentions point to a more favorable outlook than could be supported by current statistics, and likewise business sentiment seems more buoyant than actual business spending. There is no way of knowing whether inventory liquidation has run its course. On the one hand, manufacturers have apparently stopped liquidating purchased materials and goods in process. However, the inventory position of finished goods (both manufacturers' and retail) remains rather heavy.

Continuing stability in commodity prices has contrasted with the considerable rise in stock prices. The latter development may not be entirely a healthy one and may perhaps reflect fears of future inflation as much as optimism on the business outlook. Nevertheless, the stock price rise in itself probably constitutes a stimulus to greater consumer and business spending.

The latest statistics on bank credit and bank reserves are again encouraging. Total loans and investments at weekly reporting member banks recorded a sizable gain in February--a much stronger showing than in most recent years--and the comparison is favorable even if we adjust for the inclusion in February figures of a $1.1 billion sale of receivables by Sears Roebuck to the company's banks. The larger New York banks generally expect their loans to hold up well or to rise somewhat in the coming months, in contrast with declines during the corresponding period of 1958. Total reserves of all member banks, on a seasonally adjusted basis, rose substantially in February to surpass the 1960 high set in November (the gain above the April 1960 low being at an annual rate of 6 per cent); and required reserves, adjusted, reached a record high in February.

There is also considerable cause for gratification in recent developments having to do with the dollar and the balance of payments. I am thinking of such items as the sharp reduction in the gold outflow, the drying up of demand and sharp price drop in the London gold market, and the preliminary statistics pointing to the virtual cessation of the outward flow of short-term capital in January and February. However, this improvement is threatened by the atmosphere of uncertainty following the German and Dutch revaluations, and it could easily be upset by any one of a variety of developments casting doubt on our willingness and ability to follow through on the statements and actions responsible for the improvement.

Even though the business outlook is not especially encouraging, the fact that the trend is no worse than in the past few months and that we may even be seeing some faint signs pointing to recovery suggests that we can afford to continue about the same policy we have been following, without any effort to ease further. On the other hand, the banks should continue to be given sufficient reserves to meet all reasonable demands--and incidentally, with the likelihood of continuing serious unemployment even after an uptrend gets well under way, it would seem appropriate to contemplate continuing a relatively easy policy for a longer period than may have been desirable in earlier post-war business recoveries.

Since we have made only a beginning (if a rather gratifying one) toward remedying our balance-of-payments position and the problem of confidence in the dollar, the level of short-term interest rates must continue to be a matter of primary concern to the Committee. It seems to me that policy in the next three weeks should be directed mainly to preventing any decline in bill rates and preferably to encouraging some further rise. Subject to this overriding objective, I would hope the Manager would try to preserve about the same degree of ease in the market as has prevailed in the past few weeks, again as measured by the feel of the market rather than by any particular level of free reserves. If, as seems quite possible, it proves necessary to let free reserves fall well below their recent level in order to keep bill rates from going lower, I would be quite prepared to see this happen. It is hard to predict just what will be required in the way of open market operations, since there will be important cross-currents influencing market rates, including the usual seasonal dividend and tax pressures around the middle of the month and the greater scarcity of bills which will follow redemption of the March tax bills. The Manager may be able to moderate downward pressures on bill rates by spreading purchases along the maturity spectrum, thus making good use of the greater flexibility which the Committee has authorized him to exercise.

At the same time I hope that the coming three weeks will provide a further opportunity for cautious probing with respect to the possibilities for nudging longer-term rates in a downward direction. The desirability of lower rates to help stimulate the economy is no less now than it has been. I am very glad that the Manager has moved with such care and moderation in this program, and I have no dobut that he will continue to do so. I think the System has made a good start toward demonstrating that it can operate in intermediate and longer-term governments in a more or less "routine" fashion, without upsetting the market or entrapping itself in any sort of pegging operation. But it is obvious that much more time and much more testing will be needed before the policies we have adopted can be said to have had a fair trial--and I believe the Committee agrees that a fair trial is what we must seek, now that we have set our course.

Incidentally, I feel strongly that many of the press comments on the new policy have been ill-informed and have been critical on the basis of gross misinterpretation of our intentions. I would hope that all parts of the System would share in the important job of education that must be done if we are to minimize this critical attitude and provide a reasonably objective atmosphere in which to carry out our probing operations. Furthermore, I think it is essential, if our operations outside the short-term area are to make the maximum possible contribution to the economy, that the authorization for these operations be as broad as possible. To allow the public to think that they have been authorized merely as a "temporary aberration" would be to hobble their effectiveness from the start, as I believe was explicitly recognized at our last meeting.

As for the discount rate and the directive, there appears to be no reason to consider a change at this time.

Mr. Johns reported that within the St. Louis Reserve Bank there was some feeling that the forces of economic contraction might be losing some of their energy and that possibly a turnaround in economic activity might be imminent. He expressed the hope that it would be possible for the Committee to continue, as it had been doing recently in modest degree, to encourage monetary expansion. In saying this, he wished to emphasize that he was speaking of expansion in most modest terms; he was not advocating that the Committee proceed recklessly and in terms of large increments. He would hope, of course, that this could be accomplished within the interest rate objectives the Committee had adopted, and he was encouraged to believe that this might be possible.

Mr. Bryan stated that at a briefing session last Friday the staff of the Atlanta Bank was able to point out a few Sixth District economic series that had actually turned upward, and there were several others where the rate of change downward had slowed markedly. There appeared to be a prevailing note of optimism on the part of the staff and, except for the State of Florida, this note of optimism seemed to be fairly general throughout the District. He shared the staff's feeling that the economy might be bottoming out, or at least that there was no great danger that the recession would turn into an accelerating slide.

Turning to policy, Mr. Bryan indicated that, like Mr. Johns, he would favor a continued modest encouragement of monetary expansion. He did not believe that at this stage there was any danger of inducing inflation by a very modest monetary expansion. In his view, the Committee's prime concern should not be the short-term rate, but rather the encouragement of economic recovery. The short-term rate was an important factor, but it should be of secondary concern. If the Committee should get hypnotized by the short-term rate, it might easily fall into errors of policy.

Mr. Bopp stated that, along with the fragmentary glimmerings of optimism appearing on the national scene, there were a few hopeful signs in the Third District. Steel production had increased a little in recent weeks and department store sales had improved somewhat, as had freight car loadings. While unemployment claims were still high, they indicated that unemployment might not be as severe as in 1958.

In commenting on the monetary situation, Mr. Bopp said that despite decreases in bank credit and deposits since the beginning of the year, bank data in the District still reflected the influence of credit ease. The declines seemed not to be as pronounced as might be expected at this time of year. Reserve city banks had begun borrowing again on a small scale and country banks continued to borrow. One reason for the latter was that State funds for fourth class school districts had been somewhat delayed and school authorities were forced to borrow from their local banks.

Mr. Bopp expressed the view that the slight promise of improvement in the economy was not adequate to support any change in the over-all degree of ease. Attention should continue to be focused on open market operations in maturities beyond the short-term area. These had been handled skillfully and the results thus far were gratifying. Even this early in the game, however, it might be well to caution against expecting too much. Some of the conditions under which the operations were being conducted were unfavorable, and the fact that they were necessarily experimental made it more difficult to achieve the desired results. The market clearly had a "show me" attitude. A second disadvantage was the stage of the cycle in which the experiment had been begun. If it turned out that the operations had a limited effect in lowering long-term rates, this might not necessarily indicate that similar operations could not be more successful in an earlier phase of recession when expectations of lower rates were greater and when, in fact, lower long-term rates might be more effective in stimulating the economy.

In general, Mr. Bopp said, he would continue the present degree of ease.

Mr. Fulton reported that in the Fourth District insured unemployment had increased more than seasonally and was widespread. The unemployment situation was reflected in the number of cities in the District, both large and small, that had been classified as areas of substantial labor surplus. Coal production had edged down to an all-time low, and electric power output was substantially below a year ago. Auto sales declined in January, and it seemed there was no pick-up in February.

While department store sales in the past two weeks had been above the year-ago levels, for the year to date sales were 3 per cent under a year ago.

The steel industry, Mr. Fulton said, continued in the doldrums. Orders from the automotive industry were almost nonexistent, and those orders already on the books were being pushed back for delivery at some later date. However, some orders from other users of steel had been coming in on an emergency basis. If the steel they wanted was on the dock, a sale was made; if not, they went elsewhere. Inventories of steel users apparently were being kept at minimum levels, and their purchases of steel seemed to reflect that situation rather than any pickup in orders. Auto production was of course at a considerably depressed rate; the dealers were caught in a profit squeeze, with too much inventory for them to move successfully. The current feeling in the steel industry was that the automobile situation would not improve to any great extent until the fourth quarter of the year, when new models might give a stimulus to sales. The profit squeeze continued to be a severe problem in many industries, particularly in the steel industry, which had another contractual wage increase coming up in October. While they were able to absorb the increase last December, they did not think they could do so next time.

In summary, Mr. Fulton said, the situation in the Fourth District was far from bright. Perhaps the most optimistic factor was that although capital spending plans were somewhat less in dollar amount than last year, there had been few cut-backs in the planned expenditures. Also, inventories of heavy finished goods had been reduced somewhat.

In terms of policy, Mr. Fulton indicated that he would favor a continuation of the degree of ease that had prevailed recently. He was hopeful that the degree of ease would not be reduced precipitantly, thus depriving the market of funds. He continued to hope that the directive would be changed to provide for fostering "recovery" rather than "sustainable growth."

Mr. King said it was tempting to speculate on exactly what stage of the cycle the economy was in at the present time. However, this was clearly not a time to make any significant change in System policy. After commenting on the unemployment figures and the significance he attached to them, Mr. King said it was quite evident that economic recovery was not yet in progress. Consequently, from the point of view of monetary policy he saw little point in trying to make a case that the recession was bottoming out or that a turnaround might be near. Concerning the bill rate, he had expressed the view in the past that the System could get quite a bit of mileage out of a bill rate increase, and he now felt that the System had gotten considerable mileage out of the rise of the bill rate that occurred. As to the experimentation in longer-term securities that the Committee authorized on February 7, he wished to say for the record that he would have concurred in that action had he been present at that meeting. If the Committee was going to give the experiment a fair chance to succeed, he felt there had been few cut-backs in the planned expenditures. Also, inventories of heavy finished goods had been reduced somewhat.

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