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, May 8, 1962, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Balderston
Mr. Bryan
Mr. Deming
Mr. Ellis
Mr. Fulton
Mr. King
Mr. Mills
Mr. Mitchell
Mr. Robertson
Mr. Shepardson
Mr. Treiber, Alternate for Mr. Hayes

Messrs. Bopp, Scanlon, Clay, and Irons, Alternate Members of the Federal Open Market Committee

Messrs. Wayne and Swan, Presidents of the Federal Reserve Banks of Richmond and San Francisco, respectively

Mr. Young, Secretary
Mr. Sherman, Assistant Secretary
Mr. Kenyon, Assistant Secretary
Mr. Hackley, General Counsel
Mr. Noyes, Economist
Messrs. Brandt, Furth, Garvy, Holland, Hostetler, Koch, and Parsons, Associate Economists

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

Mr. Francis, First Vice President, Federal Reserve Bank of St. Louis
Messrs. Sanford, Eastburn, Ratchford, Baughman, Jones, Tow, and Coldwell, Vice Presidents of the Federal Reserve Banks of New York, Philadelphia, Richmond, Chicago, St. Louis, Kansas City, and Dallas, respectively
Mr. Stone, Assistant Vice President, Federal Reserve Bank of New York
Mr. Eisenmenger, Acting Director of Research, Federal Reserve Bank of Boston
Mr. Sternlight, Manager, Securities Department, Federal Reserve Bank of New York
Mr. Runyon, Economist, Federal Reserve Bank of San Francisco

Upon motion duly made and seconded, the minutes of the meeting of the Federal Open Market Committee held on March 27, 1962, were approved.

Before this meeting there had been distributed to the members of the Committee a report on open market operations in U. S. Government securities covering the period April 17 through May 2, 1962, and a supplementary report covering the period May 3 through May 7, 1962. Copies of both reports have been placed in the files of the Committee.

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

The money market remained generally steady during the past three weeks. Federal funds traded for the most part between 2-1/2 and 3 per cent, with the bulk of trading on most days at the 2-3/4 per cent level.

The Treasury's refunding operation was a very successful one, with attrition something less than 9 per cent of public holdings of the issues eligible for the exchange. With the completion of the refunding operation, and barring unforeseen developments, the Treasury should be out of the market at least until late June and possibly until early July. Moreover, we may,

for the time being, at least, have come to the end of the weekly additions of $100 million to the regular bill issue, since each regular issue is now up to $1.8 billion. When one considers that last week's refunding operation was the eighth Treasury financing operation thus far in 1962 apart from the weekly bill auctions, and that in those auctions an aggregate of $1.3 billion bills was added to the three-month issue, the prospective absence of the Treasury from the market over the weeks ahead should provide a welcome respite.

While dealer positions in Government securities have been reduced in the past few days, they nevertheless continue relatively heavy, particularly in the case of short-term issues. Early last week, when dealers were acquiring large amounts of rights while the subscription books were open, their positions reached what may well be an all-time high of about $4-1/4 billion. Dealers' use of credit also expanded considerably. The New York banks, however, were readily able to accommodate this bulge in credit demands, in part because individual income taxes flowed into the Treasury's balance at the Reserve Banks at a rate much faster than anticipated, and in order to prevent that balance from rising too far a succession of large redeposits, aggregating more than $1 billion, was made in the "C" depositary banks at about the same time that dealer credit demands were rising so sharply. Beginning yesterday, some of these redeposits were recalled, and more may be recalled over the next few days. At the same time, as I indicated earlier, dealers' positions, and their use of credit, have receded from the peak reached during the refunding. I might mention that despite the substantial redeposits that were made, the Treasury's balance at the Reserve Banks ran higher than had been anticipated, and this higher balance was a major factor in producing the lower-than-expected free reserve figure of last week. Largely because of the heavy redeposits into the "C" depositary banks, however, the money market tended to be somewhat easier, even with the lower free reserve figure, than it had been during the preceding two weeks when free reserves were about $100 million higher.

I should call the Committee's attention to the fact that in yesterday's Treasury bill auction a major New York bank submitted a tender for $400 million three-month bills at what seemed at the time to be a relatively high price. The strength of that and other bidding was such that that price turned out to be the lowest at which tenders were accepted, and the bank concerned was allotted $356 million on its tender. With such a large amount going to one institution, several other large banks and dealers received no awards of three-month bills at all, and others won only small amounts. The efforts of these banks and dealers to cover their commitments to customers and to establish trading positions in the new three-month bills is in all likelihood putting considerable downward pressure on bill rates at this moment.

Thereupon, upon motion duly made and seconded, the open market transactions in Government securities during the period April 17 through May 7, 1962, were approved, ratified, and confirmed.

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

At the outset it can be said that there has been no marked change in the over-all economic situation since the last meeting. On balance, economic conditions may be characterized as having continued to improve moderately. March housing starts, which I singled out as an important missing link in the data available last time, turned out to be high--back up in a single month to almost the level that prevailed before they turned down last fall. The McGraw-Hill survey of proposed plant and equipment expenditures for the current year has also become available since the last meeting. The prospective increase over last year of 11 per cent was up substantially from the 8 per cent reported in the Commerce-S.E.C. survey earlier in the year.

But there has also been some less favorable news. While first quarter corporate profits show large gains from the depressed levels of a year ago, they were probably down from the fourth quarter, even after allowance for normal seasonal difference. The stock market has experienced a considerable downward adjustment, perhaps greater than the profits figures alone would justify. We have also learned that new orders for durable goods in March declined further, by 3 per cent.

However, most of the information that has become available reflects no change or further moderate improvement. Neither the production index nor total retail sales for April have been released, but both are likely to be up a little. The unemployment rate in April was substantially unchanged, the actual reduction being just about the normal seasonal improvement.

The economy has clearly emerged from the winter lull on the up side--as almost everyone expected that it would--but it still has not shown enough strength to suggest a quarter-to-quarter change in the present quarter equal to that anticipated before the turn of the year, much less enough to make up the short-fall in the first quarter. To be more specific, the most optimistic appraisal of the current quarter would be for an increase in GNP of about $10 billion, while a rise of $13 billion was assumed in the $570 billion annual average projected in the Budget and the Economic Report.

It is always a temptation to try to find something new to say about the economic situation, either in words or in substance; but at this juncture, the facts seem to demand a repetition of the colorless phrase--continued moderate improvement.

I believe the implications of this situation for monetary policy are evident and equally colorless. Credit markets have eased further in recent weeks, as Mr. Koch will report in more detail. With Treasury operations confined largely to refunding and a large flow of savings through financial intermediaries, this easing has been the result of the normal operation of market forces, modified by the efforts of the System and the Treasury to maintain the level of short rates. Whether the endeavor to avoid downward pressure on short-term rates should be continued--or perhaps even intensified--is a question that must be answered on the basis of judgments that extend well beyond the limits of the domestic economic situation. On the other hand, domestic economic conditions certainly suggest, and might almost be said to dictate, that the easier conditions which have developed in the intermediate and long-term markets should not be frustrated by overt action at this time.

Mr. Furth presented the following statement with respect to the U. S. balance of payments and related matters:

Our international deficit dropped sharply in April, according to tentative and partial data, perhaps back to the annual rate of $1-1/2 billion that prevailed in January and February.

Satisfaction with this improvement should be tempered, however, by the suspicion that some of it may have reflected movements of capital from Canada. For reasons of economic analysis or because of some leakage of official secrets, the market had apparently expected that Canada would establish a value for its dollar at a rate lower than the current quotation. Market offers of Canadian dollars began greatly to exceed market demand, and the Bank of Canada lost more than $100 million during April in its attempts to maintain the quotation at a figure 2-3/4 per cent higher than the par value declared on May 2. Under these circumstances, the reflux of funds to Canada, which should promptly occur if the market is satisfied with the viability of the new par value, might soon increase our deficit. Further data will be needed, however, before our balance of payments for April can be firmly analyzed.

The international situation still shows continuing or even accelerating expansion in Western Europe and little change

elsewhere. But four recent financial decisions of foreign monetary authorities are likely to exert some influence on our international accounts.

The first and most important of them was the reduction in British Bank Rate. Initially, at least, this reduction seems to have put an end to the accumulation of dollars by the Bank of England. This change has lessened the threat of further gold drains. Since most of the funds that had flown to London came from Continental Europe, however, the cessation of the flow does not directly improve the U. S. balance of payments.

Furthermore, the reduction in British interest rates has not widened the covered interest-rate differential on Treasury bills in favor of New York, but on the contrary has led to its disappearance. Renewed market confidence in the future of sterling, bolstered by the repeated reductions in Bank Rate, has caused the forward discount of sterling against the dollar to drop from nearly 2 per cent to little more than 1-1/4 per cent. This drop was greater than the decline in British Treasury bill rates following the Bank Rate change.

The second action was the decision of the Netherlands Bank to increase its discount rate and to permit this year only nominal foreign bond issues in the Amsterdam market. While these moves are likely to have only negligible direct effects on the dollar, they illustrate the tendency of European authorities to restrict international capital movements without giving much consideration to the principles of inter-central-bank cooperation. Netherlands officials have repeatedly urged the United States to raise interest rate levels in order to force foreigners to shift their borrowing to Continental Europe. Interest rates in New York are higher than in Amsterdam, but the differential cannot benefit our capital accounts as long as foreign borrowers are prevented from taking advantage of the lower Netherlands rates.

In a similar vein, the German authorities have followed up their expressions of concern about inflationary pressures by not only raising Treasury bill rates but also permitting German banks again to pay interest to foreign depositors. These actions were taken despite the jump in the German trade surplus in March to an annual rate of $2 billion, twice the January-February rate. European surplus countries hardly make it easier for the United States to eliminate its external deficit when they take immediate corrective action as soon as their surplus shows the first signs of declining.

The fourth action was the establishment of the new par value of the Canadian dollar. The abandonment of the flexible exchange rate experiment has been acclaimed in Washington, but

there has been some uneasiness about the magnitude of the depreciation of the Canadian dollar. The new low rate may well adversely affect our trade as well as our capital accounts.

The position of the dollar has not changed much in gold and foreign exchange markets. The gold price in the London market has remained in the neighborhood of $35.08; at least part of the time, the Bank of England has probably been able to act as net purchaser rather than as net seller of gold. The dollar has slightly improved against sterling and against the German mark. But it has declined against the Swiss franc and, probably as a consequence of the actions of the Netherlands Bank, against the Netherlands guilder; it is now virtually at the floor in the Netherlands, as it has been for some time in the two major surplus countries, France and Italy.

None of these exchange rate movements, however, seems to have been caused by anything resembling a flight from the dollar. The market may agree with those economists who believe that the fate of the dollar will mainly be decided by economic and financial developments in the United States, and that these developments have so far not justified apprehension regarding our ability to maintain stability in our cost and price system.

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

In commenting on recent financial happenings this morning, I should like to focus on those developments that we have on occasion in the past referred to as the intermediate objectives of Federal Reserve policy. First, let us look at various concepts and forms of liquidity. Money supply, narrowly defined, has picked up smartly in recent weeks. After increasing $300 million in March, it rose a billion dollars in April. It is now 2-1/2 per cent above the level a year ago.

The sharp growth in time and savings deposits at commercial banks continued during the first half of April, but apparently tapered off somewhat thereafter. Nevertheless, growth in total deposits at commercial banks, expressed as a seasonally adjusted annual rate, has been at about 10 per cent since the first of the year. There is also some evidence that the hectic activity in time accounts is slowing down. The data collected by the Chicago Federal Reserve Bank on gross new deposits in and withdrawals from these accounts at banks in the Seventh District show both declining quite sharply in recent weeks. Forms of liquidity other than deposits at commercial banks have also apparently increased significantly further, although no data are available subsequent to March.

Such over-all liquidity ratios as that of total liquid assets to the gross national product and that of corporate liquid assets to current liabilities, however, are still not high by historical standards. With reference to the state of the economy's liquidity and its relevance to activity, a new concept that came to my attention the other day was that of net private financial assets to GNP. This concept subtracts private financial liabilities from liquid assets. When one makes this adjustment, he finds that liquidity has declined much more sharply relative to the size of the economy since World War II than is shown by the more usual liquidity ratios, and also that it is currently at a lower level.

Turning from liquidity to credit availability as another indicator of the effects of recent Federal Reserve policies on economic activity, total bank loans and investments were up 8 per cent in the first four months of 1962 on a seasonally adjusted annual rate basis. The sharpest increase has been in bank holdings of securities other than U. S. Governments, presumably mainly municipals, which have increased at over a 25 per cent annual rate. The rate of increase in business lending has slackened somewhat, whereas the rates of increase in real estate and consumer lending have picked up thus far this year.

The volume of capital market financing has also accelerated in recent weeks. New corporate security issues totaled $1.2 billion in April, up from an $800 million monthly average in the first quarter and less than the heavy April 1961 calendar only because of the large AT&T financing a year ago. Municipal financing totaled about $850 million in April, approximately equal to the first quarter average, but somewhat above the year-ago level. The volume of both corporate and municipal financing, however, is expected to decline this month.

As a final indicator of Federal Reserve effects, working of course along with all of the various market forces, the cost of credit has continued to decline, particularly in the case of long-term financing. The Government bond rate and that on outstanding Aaa corporate issues, at 3.87 and 4.31 per cent, respectively, are now at around their lowest levels since last summer. New corporate issues are coming to market at about their lowest rates since 1958.

The rate on outstanding new Aaa municipal issues, at 2.93 per cent, is also at the lowest level since 1958. Other signs of the recent easing tendencies in long-term financing are the facts (1) that interest rates on new corporate issues are below those on outstanding issues, a rare occurrence, and

(2) that the rate on lower grade municipal issues has declined considerably more sharply than that on higher grade issues.

I should like to conclude this morning with a few comments on recent projections of economic and financial developments for the rest of 1962 made by several of my colleagues here at the Board. A more detailed presentation of their findings will be given this afternoon to those of you who are interested.

The authors conclude that a reasonable case can be made for either (1) a continuation of recent experience, thus meaning further expansion in GNP at, let us say, a 5 per cent annual rate, or (2) a pickup of the rate of expansion to the path projected in the last Budget message, which would imply GNP increasing at a 7-1/2 per cent rate. The lower model would likely leave us with unemployment and capacity utilization rates at about the same levels as at the beginning of the year. The more optimistic model would mean that some progress would likely be made in our resource utilization problem, but at still a surprisingly slow rate. In neither model does the rate of resource utilization suggest upward price pressures in commodity markets this year.

For our more immediate purposes, the main relevance of the projections is that neither of the models suggests that any sustained upward pressure on interest rates is likely in the months ahead. In the case of both projections, credit demands would be only moderate relative to the size of the economy, although in dollar amount the total funds raised in credit and equity markets might approximate the level reached in 1959. The moderate nature of likely prospective credit demands is also suggested by the recent McGraw-Hill survey of business plans for capital spending, which found that companies expect their demands for external funds for all purposes to increase only 1 per cent over last year, whereas internal funds are expected to rise 14 per cent.

Savings flows, on the other hand, are likely to remain relatively large throughout the rest of 1962 and, assuming the continuance of monetary ease, the vast bulk of these flows would likely be channeled through financial intermediaries rather than directly into financial markets. Moderate credit expansion, large savings flows to institutions, and continued monetary ease are the basis for the projection of relatively stable interest rates under the optimistic model and possibly even further declining rates in the lower model.

Neither model suggests the need or desirability of any near-term lessening of ease in monetary policy--not, at least,

until or unless the effects of policy become more obviously adverse, either with respect to capital outflows or with respect to a marked deterioration in bank lending and investing activities. On the other hand, April developments in liquidity, credit availability, and interest rates suggest to me that the degree of ease being achieved by existing policy is for the present providing an adequate monetary stimulant to economic activity.

Mr. Treiber presented the following statement of his views on the business outlook and monetary policy:

It is now clear that the slowdown in economic expansion at the beginning of 1962 was only a pause. The expansion has resumed at a moderate pace.

Consumer spending, especially on automobiles and residential construction, has risen.

The McGraw-Hill spring survey of businessmen's spending plans for 1962, made before the steel price episode, indicates, as expected, a somewhat faster growth in expenditures for plant and equipment for the balance of the year than was indicated in a survey taken two months earlier. While the prospect of a cost-price push in the steel industry has been avoided, a substantial part of the business community disliked the Administration's role in getting the steel price increase reversed. With many businessmen questioning the Administration's attitude toward business, will these questions and doubts have a dampening effect on the spending decisions of businessmen? Corporate profits have been rising, and greater profits encourage greater capital expenditures. I would conclude that, despite the fears and hesitations of some businessmen, we may expect to see increased spending for capital purposes as indicated in the survey.

The problem of unemployment persists. The rate of unemployment is still significantly higher than in the comparable stage of the two previous business expansions. Despite the drop in total unemployment, the number of persons out of work more than half a year (the so-called "hard core" unemployment) is well above the trough of the recession in early 1961.

The expansion in business activity continues to be accompanied by price stability.

Bank loans have shown moderate strength in recent weeks. Consumer loans and loans connected with real estate and construction have shown substantial strength. The money supply

had grown in April by a larger amount than in recent months, while there are some indications that the growth of time deposits is slowing down.

The banks still have adequate liquidity. This is also true of other segments of the economy.

The Treasury will be completing its current refunding operation on May 15. Thereafter, there will be a period of several weeks during which the Treasury will not be coming to the market except to roll over the weekly Treasury bill issues. It is not expected to need cash until July, although the Treasury may meet some of its July needs through an operation in late June.

The balance-of-payments problem continues with little or no improvement. Indeed, the statistics for the first quarter of 1962 are worse than those for the first quarter of 1961, and even more so if a technical adjustment in German balances is disregarded.

Assuming a continued expansion of business activity in the United States, imports are likely to move up further, thereby worsening our payments position. We must also be alert to the risk that at some point continuing deficits and the absence of what foreigners would regard as a coordinated and determined effort to cope with the problem may so disturb foreign confidence as to lead to large-scale shifts from dollars into gold. Our gold loss this year has exceeded that of the comparable period in 1961: and further losses are to be expected.

In considering relative interest rates in international markets, we have been accustomed to concentrating on the short-term rates and their influence on short-term capital movements. Long-term rates, of course, also have an influence. The relatively low long-term interest rates in the United States certainly have been an increasing encouragement to long-term borrowing by foreigners in this market.

In considering monetary policy, it is apparent that the domestic economic situation is improving while the international financial situation is bad and is likely to continue to be so. Under the circumstances, it seems to me that, with increased economic activity over the coming months, cyclical forces, as they develop, should be allowed to put some upward pressure on market rates--both short-term and long-term--and to reduce free reserve positions. This should help to check undue acquisition of long-term issues by commercial banks and to counteract any speculative expectations that might be developing with regard to long-term Government securities; it may also

> dampen speculative real estate developments which are undertaken here and there. I would not expect that some tightening would sap the mortgage market and curtail construction activity, nor would it significantly curtail capital spending. On the other hand, it might dampen to some degree the outflow of long-term capital.
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> Settlement for the new issues in connection with the current Treasury financing operation will take place next Tuesday, May 15. In the meantime, I think the Desk should resist any significant downward movement in Treasury bill rates, even if this should involve some shrinkage in free reserves. After the refunding is out of the way, I would favor probing toward a somewhat higher level of short-term rates. I would not stand in the way of any moderate upward movement in rates that might come about through the action of market forces.
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> I think it would be desirable to make some changes in the current economic policy directive, which for some time has referred to "the modest nature of recent advances in the pace of economic activity." It would seem desirable to revise the first paragraph of the directive so as to reflect the current economic situation. I think it would also be desirable to revise the second paragraph so as to indicate that the System would not resist some moderate upward pressures brought about by continued business expansion.
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> I would not favor overt action by raising the discount rate at this time unless, of course, it were part of a "package" or a coordinated group of actions to be taken by our Government on several fronts to focus attention on and to help solve our balance-of-payments problem.

Mr. Ellis reported that New England had been enjoying good spring weather. However, the strength of the economy seemed to have a deeper base than good weather. The economy was being assisted by consumer spending, and the willingness to borrow had improved. Easter season retail sales, seasonally adjusted, were some 10 per cent ahead of 1960, the previous high year. The ski resort business exceeded the previous record year of 1960, and automobile sales continued strong. Major reporting banks indicated that purchases of new cars were some 18 per cent

above a year ago, as measured by their extensions of installment credit. Construction in the greater Boston area was getting a strong boost from several exceptionally large projects that were all in progress at the same time. The New England production index moved up slightly from February to March, with the important strength in the durable goods industries. In summary, economic expansion was proceeding at a modest pace, although the picture was somewhat mixed.

First District reporting banks continued to experience a business loan demand that was a little stronger than seasonal expectations. During the most recent three-week period, time deposit growth slackened. Yet savings banks had a deposit growth running some 8 per cent ahead of a year ago, while withdrawals were down about 2 per cent.

Turning to policy considerations, Mr. Ellis referred to comments in Mr. Noyes' statement to the effect that there had been no material change in the business picture, which was basically one of continuing modest improvement. This improvement was more evident, Mr. Ellis suggested, in data on final takings at consumer, business, and Government levels than in production and employment series. Looking back, he felt that monetary policy had quite properly been stimulating. If he understood Mr. Koch's figures correctly, there had been fairly sharp increases recently in the measures of money supply and credit availability. These developments would appear to reflect the effect of monetary policy, which comes with some lag in a period when demand is strengthening. If there continued to

be a strengthening in demand, he would expect the expansion in the credit series to be more rapid than one would want to accept on a continuing basis. With reference to the two models of economic and financial developments for the rest of 1962, to which Mr. Koch had referred, he had some feeling that if the economic advance should gain momentum a monetary policy designed to preserve free reserves of around $400 million would support a credit build-up more rapid than the Committee would like to see continue.

Mr. Ellis expressed the view that no abrupt shift in policy was warranted at this particular time. He agreed with Mr. Koch that the present degree of ease was providing an adequate monetary stimulant to economic activity. At the same time, he would be prepared to revert to the position taken by some in January, before the pause in business expansion, that the System should think in terms of allowing a strengthening of credit demands, if and when they developed, to create conditions of less market ease. The expansion of the domestic economy seemed to provide greater leeway for monetary policy to make whatever contribution was possible so far as the international situation was concerned. This suggested to him that the projections of required reserves should be formulated on the basis of an annual growth rate of 3 per cent, or somewhat less, rather than 4 per cent. He would be inclined to accept a target for free reserves in the area of $350-$400 million and to allow short-term rates to push toward 3 per cent, with the Federal funds rate

more frequently at 3 per cent. He would anticipate some member bank borrowing, which should be taken as evidence that the initiative in credit tightening was coming from the market place as the result of demand forces. While his prescription was presented within the general framework of no substantial change of policy over the next three weeks, he would suggest that doubts be resolved on the side of a little less ease.

Mr. Ellis expressed the view that it might be appropriate to change the first paragraph of the current economic policy directive, but he would be inclined to leave the second paragraph as it stood. He would not recommend changing the discount rate at this time.

Mr. Irons reported that in the Eleventh District the over-all picture was one of moderate, generally satisfactory improvement. The employment situation was strong, department store sales during the Easter period were up about 8.5 per cent from the previous year, and construction was running about 35 per cent above a year ago. Unemployment, on an unadjusted basis, stood at about 4.9 per cent of the labor force. There was no appreciable change in the petroleum situation. The industrial production index, heavily weighted for petroleum, was down in March but appeared likely to show some improvement in April. Agricultural conditions were generally good, but with some spottiness, as is often the case at this season of the year.

Loans and investments of District banks were up moderately. The banks had been tending to reduce their holdings of short-term Governments and to buy longer-term Government and other securities. Total deposits were up, the rise in time deposits being appreciably greater than the decline in demand deposits. During the past three weeks District banks were net buyers of Federal funds, while borrowing from the Reserve Bank was nominal.

With respect to monetary policy, Mr. Irons said it seemed to him, upon evaluating the economic situation, that it would be appropriate to continue about the same policy that had been followed during the past three-week period, in fact the past several periods. There was an absence of inflationary pressures. Also, there appeared to be considerable uncertainty among businessmen in the Eleventh District since the steel price episode in terms of the outlook for business. There was some concern about the profit-wage-price situation, and how this would work out. As to economic activity, there seemed to be steady improvement, but at only a moderate rate. Accordingly, as he had said, he would continue about the same degree of ease that had prevailed recently. The System should continue to provide reserves, but it should not force them on the banking system. There had been stability in the Federal funds market during the past three weeks, and also relative stability in the bill market. It appeared that reserves had been adequately available because bill rates did not move up; it

also appeared that the degree of ease was not particularly excessive because short rates did not move down appreciably. He would suggest continuing to watch the tone and feel of the market closely, with a view to maintaining a comfortable but not an excessive degree of ease. If the drift should be toward a little more firmness as the result of market forces, he would not be too concerned. As rough targets, he would suggest a Federal funds rate from 2-1/2 to 2-3/4 per cent, free reserves in the area of $350-$400 million, and a bill rate around 2-3/4 per cent or on the up side. The kind of policy that he had been suggesting in general terms should come out to about that sort of picture.

Mr. Irons said he had not thought in terms of changing the current economic policy directive at this time, partly because he felt that present policy should be continued and partly because he did not see enough change in the domestic or international situation to establish any compelling need for altering the descriptive phrases in the directive. On the other hand, he would not oppose making some modest changes in the directive if they were felt desirable by the Committee. He would not recommend changing the discount rate at this time.

Mr. Swan said that very little in the way of new Twelfth District statistics had become available since the April 17 meeting. As he mentioned at that time, preliminary data had indicated that the seasonally adjusted unemployment rate in the Pacific Coast States in

March was not as favorable as the national rate. That had now been confirmed. In fact, the rate rose a little from February to March. However, consumer spending continued strong and major construction contract awards were up sharply in March from the low February level. For the first quarter, construction contract awards were up 4 per cent from the corresponding period of the previous year. Gains larger than 4 per cent in residential and private nonresidential awards more than offset a sharp decline in utilities and public works contracts. However, a rather widespread labor dispute in northern California tended to cloud the near-term outlook.

For the first three weeks of April, District reporting banks continued to show a considerable increase in real estate loans, as they had for several weeks previously, and a smaller increase in commercial and industrial loans. The large banks were still net sellers of Federal funds. Savings deposits at weekly reporting banks were down during the three weeks ended April 25, the first time that a decline had occurred this year. Presumably the decline was related to income tax payments. During that three-week period, incidentally, there was a small decline in savings deposits at all weekly reporting banks throughout the country; however, due to the rather substantial decline in the Twelfth District, there was actually an increase in the remainder of the country. Five out of seven major Los Angeles and San Francisco banks indicated that they experienced a fairly significant decline in earnings during the first quarter of this year. The only two that did not had already gone on a daily interest basis in the first quarter of 1961.

Turning to the national outlook, Mr. Swan noted that economic expansion, though continuing, was not vigorous. The economy still had a considerable way to go before reaching a satisfactory relationship to capacity in terms of equipment or manpower, and apparently quite a way to go before price pressures were created. There was an excessive level of unemployment, and this problem might become even more difficult if there should be a resumption of growth of the labor force. Thus, it seemed to him that as of today, there was no basis for even a slight tightening of policy. Nor did he believe that the recent decline in long-term rates--which reflected market factors rather than System policy--or the international situation provided sufficient reason for tightening. The best inducement for funds to remain in this country rather than move abroad was a higher level of business activity in the United States.

Consequently, Mr. Swan said, he would recommend no particular change in policy at this time, and if anything a leaning on the side of slightly more ease rather than less. This would mean retaining the 4 per cent growth target in terms of total reserves, or moving the target a little higher. As to free reserves, he would move up a little from the $400 million average of the three weeks ended May 2. He would not be particularly concerned if the bill rate fell somewhat below 2-3/4 per cent.

As to the current economic policy directive, Mr. Swan said he was rather surprised at the suggestion to change the first paragraph, because he thought the language of the existing directive was still an apt description of the current economic situation. He would not recommend any change in the discount rate at this time.

In a further comment, Mr. Swan inquired whether there was not an increasing tendency to use repurchase agreements, in lieu of outright purchases, when providing additional reserves, presumably to minimize direct downward pressure on the bill rate. While he could appreciate that this might be a useful device, it seemed to him this was a departure from the original purpose of the use of repurchase agreements. Since the option of withdrawal before maturity was with the borrower, this tended to take the initiative away from the Open Market Account to some extent. Of course, if repurchase agreements were withdrawn, presumably they could always be replaced by outright purchases of securities. Nevertheless, he wondered if the use of repurchase agreements did not encourage falling short of the estimates at the end of a week when this happened. To repeat, he felt that there had been some shift from the original purpose of repurchase agreements, which he interpreted as contemplating a device to provide additional reserves in the event of temporary tightness or knots in the market, to a more significant and more frequent role in open market operations. It seemed to him that the choice was present, when

there were advance withdrawals, of whether to make a substantial entry into the market by purchasing a greater amount of securities than might be desirable, in terms of a given day, or of falling short of the target for the reserve position of the banking system. The foregoing was more in the nature of an inquiry than a critical comment, but he had wanted to raise the question.

Mr. Deming stated that there was little new to report from the Ninth District, which appeared to be moving along about the same as the nation. The only item that showed any real difference from the nation was loan demand, which was somewhat stronger in the District. This had been the case at city banks of the District during most of the current year. Bankers were talking about the demand being brisk, or quite good, and these comments did not seem characteristic of those being made by bankers throughout the country generally.

As to the national situation, Mr. Deming noted that the rate of economic gain was characterized as modest. That was probably correct. However, the rate of expansion did not seem to be too bad; current estimates of gross national product for the second quarter did not appear to be substantially below the rate that had been projected at the beginning of the year. At the same time, from his observations and contacts, he did not sense any feeling of exuberance. According to the projection models to which Mr. Koch had referred, it would seem doubtful whether natural forces were going to produce any substantial

market tightening; if he understood correctly, even the more optimistic model did not contemplate a strength of demand for funds such as to have much effect on interest rates. If that was true, the only way that a tightening could be achieved would be through overt action, and he would not be prepared to suggest such action at this time.

Summarizing, Mr. Deming said he did not believe that any particular change in the course of policy was called for in the next three weeks. He would try to keep free reserves around their recent levels. While he did not like to see the bill rate fall unduly, neither would he be particularly concerned if it fell to a somewhat lower level for a day or two, or even for a week. He saw no particular reason to change the policy directive at this time, and he would not change the discount rate.

Mr. Scanlon reported that business continued to improve slowly in the Seventh District. Department store sales and sales of new automobiles indicated that the rather strong consumer demand in March had continued in April. Production was rising gradually, but remained below prerecession levels. The decline in steel production following the wage settlement had been somewhat less in the Chicago area than in the nation. Nevertheless, although order cancellations had ended, production was expected to decline further. A recent survey indicated that farm real estate prices had risen from year-ago levels.

Mr. Scanlon commented that interest in foreign trade continued to grow in the Midwest. The relatively slow economic growth in important areas in the District seemed to have stimulated interest in the possibility of increasing exports. In view of comments heard frequently with regard to wage rates and commodity prices, it was interesting to note that there were some situations where United States manufacturers were competing on favorable terms with foreign plants. After citing certain cases in point, Mr. Scanlon commented that according to one manufacturer with plants here and abroad, the advantages of domestic production included the economies of large volume, the availability and quality of suppliers, and the availability of skilled labor. Also, Government sponsored insurance programs appeared to be playing a larger role in private plans to finance exports.

Seventh District banks, in order to offset the increased cost of interest payments on savings deposits, were lengthening the average maturities of their portfolios by purchasing longer-term Government bonds and other securities and by acquiring mortgages from the Federal National Mortgage Association.

In summary, Mr. Scanlon said, the rise in business activity at a pace below general expectations, together with the uncertainties created by the recent steel price episode and the possible effects of the Administration's proposed new international trade program, had caused some business executives to adopt a cautious attitude. With considerable

margins of unused labor and unused plant capacity, he felt that no signal should be given to the market at present that would suggest a shift of Federal Reserve policy toward less ease. In his opinion there was no need for any material change in the policy directive, and he would not make any change in the discount rate at this time.

Mr. Clay expressed the opinion that the Committee should continue essentially the same policy of monetary ease that it had been pursuing in recent weeks. While there had been further expansion in economic activity, notably in the automobile industry, a satisfactory performance of the national economy in terms of employment and output would require substantial and widespread improvement in various sectors of the economy. Expansion in bank credit on a seasonally adjusted basis and the accompanying developments that had been taking place in the money and capital markets had been appropriate to these circumstances.

A combination of various factors, including the growth of bank credit, expectations as to both demand and supply of credit, and the interest of banks in acquiring assets with higher yields to cover costs on time deposits, had produced more attractive interest rates for prospective borrowers in the important areas of business capital outlays, residential building, and State and local construction. Statements by bankers in the Kansas City District suggested that the expansion of the credit base also may have had some impact on effective consumer credit rates. These easier credit conditions should help to encourage further expansion in demand for goods and services, and monetary policy should foster their continuation.

The international balance-of-payments problem appeared to Mr. Clay to call for an extension of recent policy with respect to the Treasury bill rate--within the same general range previously determined. In line with the monetary policy he suggested, no change was recommended in the Reserve Bank discount rate.

Mr. Wayne said he saw nothing in recent Fifth District developments that differed significantly from the situation reported three weeks ago. The economy continued to plod slightly upward without unusual strength in any area. Manufacturing employment increased slightly in March, and nonmanufacturing fell a little. Furniture was still the brightest spot, but the gains were growing smaller each month. Textiles showed little change, and bituminous coal production--while improving somewhat--was still far from satisfactory. In short, the District situation closely resembled that of the nation.

Turning to policy considerations, Mr. Wayne said that as this second year of the current upswing advanced, it seemed to him there were two trends or tendencies in the economy that had real significance for monetary policy. The first was an increasing possibility that business activity would flatten out and later turn down without ever having attained a momentum which would justify or permit any significant degree of credit restraint. The second was a tendency for long-term capital outflows to continue and perhaps increase as a result of the decline in long-term interest rates. This decline had been caused to a considerable extent by the higher interest rates

on time deposits permitted by the change in Regulation Q as banks reached for investments with longer maturities. The outflow of long-term funds might be more troublesome than the movement of short-term funds since it was more permanent and not so likely to be reversed by changes in the relative levels of interest rates here and abroad. Even so, it would certainly be unwise, in view of the faltering upswing, to attempt to raise long-term rates to prevent such flows.

The dilemma was a most complex one, Mr. Wayne continued, and monetary policy could make no more than a limited contribution toward its solution. Nothing in the domestic situation indicated any need for tightening credit, and he believed that the System was doing all that was feasible on the international front. Therefore, he would suggest a continuation of present policy, by which he meant a policy of "maintaining a supply of reserves adequate for further credit and monetary expansion," and avoiding any general pressure on banks' reserve positions. This would probably require a level of free reserves substantially higher than the level inadvertently reached last week, and perhaps in the range mentioned in the discussion three weeks ago.

Mr. Wayne believed it would be appropriate to renew the present current economic policy directive, and he saw no reason to change the discount rate.

Mr. Mills said his reasoning paralleled that expressed by Mr. Treiber. It argued for coming to grips with what he believed to be an

unsatisfactory financial situation, and a shift in the course of Federal Reserve policy toward reducing the supply of reserves. Adoption of that kind of recommendation would require a modification of the current economic policy directive to reflect the shift of policy. In further explanation of his position, Mr. Mills presented the following statement:

> Monetary and fiscal policy actions going back over more than one year are responsible for critical problems that are daily coming into clearer perspective. A start toward their solution has become urgent and further delay will only complicate an already difficult situation.
>
> Massive deficit financing for the Federal Government is the crux of the problem. Official encouragement from both monetary and fiscal authorities has sponsored the commercial banking system's absorption of the past year's increase in the Federal debt. This encouragement has taken the tangible form in the area of debt management of tailoring new issues of U. S. Treasury securities so as to attract commercial bank investment as against investment by the private sector of the financial market, and in the area of monetary policy by continuously supplying reserves to the commercial banks in quantities that, in the absence of a strong loan demand, have fostered their massive acquisition of U. S. Government securities. It is significant that in dollar amount a substantial proportion of the increase in the Federal debt is now held in the swollen positions of the U. S. Government securities dealers, and has been financed on commercial bank advances. In terms of "classical" theory, the present fiscal and monetary background is suspect and its implications have been rendered more dangerous because of official support, which has instilled confidence into the minds of investors that the present financial market climate can be maintained indefinitely even though it is the artificial product of a needlessly easy credit policy that has been abetted by officially pegging an interest yield floor for U. S. Treasury bills.
>
> Foreknowledge that the U. S. Treasury will have to borrow heavily in the second half of calendar year 1962 emphasizes the urgent need for a change in the tone of Federal Reserve System monetary and credit policy that will shift its influence to the side of free market principles and thereby encourage private,

> rather than commercial bank, investment in U. S. Treasury obligations. Unless such action is taken, the risk will be run that the U. S. Government securities market will break down under its own weight, particularly because of the unwieldy positions of the U. S. Government securities dealers. Considering the degree of liquidity already injected into the economy by virtue of monetary policy actions, a moderate move toward lessening the supply of reserves at the commercial banking system's disposal would in no wise reduce general credit availability in the economy to a point that could stifle the constructive use of credit in fostering a high level of economic activity. The kind of policy shift contemplated could be expected to influence some strengthening of interest rates, which would of itself be beneficial in compelling some reduction in the positions of U. S. Government securities dealers, thereby improving their capacity to participate more broadly in financing the U. S. Treasury's prospective offerings of new securities. By the same token, commercial bank portfolios of U. S. Government securities would be jogged loose, leaving the banks in better positions to flexibly underwrite and participate in the U. S. Treasury's new securities offerings while, at the same time, the long neglected free market for U. S. Government securities would have been cultivated by the attraction of a modest increase in investment returns. The policy proposed, of course, contemplates terminating the present pegging operation with respect to U. S. Treasury bills and, needless to say, foreign observers would welcome the Federal Reserve System's action as being in accordance with accepted central banking theory and as token recognition of its part in countering the nation's balance-of-payments problem.

Mr. Robertson said he agreed completely with the views expressed by Mr. Swan. Recently, he had reviewed the policy followed by the Open Market Committee during the past five three-week periods, and he felt that this policy provided a good record. It had been successful in stimulating moderate economic growth, but there were still unutilized resources and excessive unemployment. He could see no evidence of sloppiness in the credit markets or of speculative trends. Consequently, he would have no brief for any tightening of credit at this time. Instead, he felt that

the Committee should hold close to present policy and, if anything, move slightly on the side of additional ease.

Turning to the current economic policy directive, Mr. Robertson suggested certain changes. He would make no change of substance in the first paragraph, because in his opinion the language of that paragraph described the current situation well. His only recommendation would be to eliminate the clause that called for recognizing the need to maintain a viable international payments system. That was because he did not understand its meaning. As to the second paragraph, he would revise it as follows:

> To implement the policy of the Committee, operations of the System Open Market Account shall be conducted with a view to maintaining an average level of free reserves in the neighborhood of $400-$450 million, with allowance for any uncertainties or distortions that may develop regarding current or projected reserve figures. Deviations from this specified free reserve range shall be permitted as appropriate in order to moderate abrupt or sustained changes in short-term rates or other untoward market pressures or persistent departure of adjusted required reserves against private demand deposits from the average upward trend of the past five months.

Such a directive, Mr. Robertson noted, would call for a growth of required reserves against private demand deposits at a little below an annual rate of 5 per cent. It would allow for temporary deviations that might occur accidentally while continuing to aim generally toward the prescribed target. In his opinion, such language would be more under

standable and provide a better basis for the operation of the Open Market Account.

Mr. Shepardson noted that there seemed to be rather general agreement that a modest continuing growth of the economy was taking place. In his opinion, the rate of growth was affected more by other factors than by monetary policy. There was, for example, the uncertainty of the business community resulting from the steel price situation, along with the uncertainty about wage pressures. The Government spending program also was a factor. Certainly, there was needed a fuller utilization of resources, both human and physical, but he did not feel that monetary policy could exert a significant effect. Reports on the availability of credit, the money supply, and liquidity seemed to indicate that monetary policy had done its job adequately, if not more than adequately.

Mr. Shepardson expressed concern about a continued growth of total reserves at the rate of 5 per cent. It would be preferable, he thought, if the rate of growth was more like 3 per cent, or possibly less than that. He would not interpret that as a tightening of credit, but rather as a slowing down of the rate of credit expansion.

As to the current policy directive, Mr. Shepardson suggested the possibility of a change in the first paragraph to call for "permitting" rather than "promoting" further expansion of bank credit and the money supply. As he saw it, the present wording indicated that

the Committee was trying to do too much. Its function should be to permit such expansion as might be brought about by other forces. This could come only through a revival of business confidence, which could be aided by removal of the uncertainty growing out of the steel price situation and by some different approach to Government expenditures.

Mr. King commented, with respect to the recent rise in bond prices and the weakness in the stock market, that such movements usually were associated with conditions that would suggest a shift of policy in the direction of ease instead of tightening. He did not feel that the System should provide more ease than it had provided. On the other hand, he did not think that economic conditions at the present time required any tightening. The fact that the Treasury, after another week, reportedly intended to refrain from adding an additional $100 million to the weekly bill offering was a factor with which the Account Management would have to contend. He would not want the bill rate to decline unduly, and developments would have to be watched closely. In any event, however, he doubted whether the bill rate was likely to move higher; efforts probably would have to be focused on the other side. In fact, he did not believe it would be appropriate to ask the Manager to assume responsibility for holding the bill rate at the present level. If the bill rate should fall somewhat, that might reflect forces that

were beyond the reasonable control of monetary policy. In conclusion, Mr. King said that his general views on policy were similar to those expressed by Messrs. Wayne and Deming.

Mr. Mitchell expressed agreement with the position of Mr. Swan, both in reasoning and recommendations. He would add only the comment that in his opinion the debate on policy that had been going on within the Committee for several meetings was an important one, although at first it might appear to involve degrees of difference that were very small. The question centered in the view presented repeatedly by the representatives of the New York Bank in favor of a change of policy, a change which it was indicated would be slight. In Mr. Mitchell's opinion, that point of view should be resisted vigorously until the country had approached closer to full utilization of plant capacity and labor force, and until it could be shown that the stability of the price level was threatened in some way. At this juncture, he saw no justification for a change in monetary policy.

Mr. Fulton said that the Fourth District was feeling the backlash of the steel inventory build-up. Furthermore, this situation might be prolonged for a while, as steel ingot production had not as yet adjusted to slower deliveries as customers sought to reduce inventories. As a matter of fact, the Fourth District had been lagging somewhat before the current downslide began. As to steel production, the first quarter of 1962 was quite high and satisfactory,

the second quarter would be lower than the first, and the third probably would be lower than the second by about 10 per cent. It was hoped that production would start back up in the fourth quarter. The cancellation of orders and deferment of deliveries had been general throughout most of the steel product lines, although pipe was showing a somewhat better performance than other lines. The steel companies felt, however, that the atmosphere in which their customers were working was rather good. The customers seemed to feel that business had reached a plateau from which an expansion could occur at a reasonably satisfactory pace.

Automobile sales in the major centers of the District continued to show considerable strength, although they did not measure up to the outstanding performance nationally. Including imports, sales in the nation were at an annual rate of about 7.5 million in April, causing some sources in the auto industry to raise their estimates for the year to about 6.75 million, or possibly 7 million. Inventories had been substantially reduced, and at the end of April totaled about 953,000--a 38-day supply--which was quite low for this time of year. If sales continued high, this would of course have a beneficial effect on the steel industry.

Construction activity in the District during March, as during the entire first quarter of the year, was mediocre, only 3 per cent above the year-ago level compared with an increase of 19 per cent nationally. Insured unemployment had declined considerably more than

seasonally, but the improvement seemed to have tapered off, especially in the steel centers. Nonfarm employment was still below pre-recession levels. Department store sales were estimated to have declined slightly in April after seasonal adjustment.

Bank credit had expanded somewhat, with the increase divided about equally between loans and investments. Investments reflected a lengthening of maturities, and business loans had declined.

All in all, Mr. Fulton said, no ebullience was seen. He believed that the degree of ease provided by the Committee had been appropriate, and he would continue it. He would not change the current policy directive, feeling that any revisions would necessarily be minor and would amount only to changing words. He would not favor a change in the discount rate.

Mr. Bopp reported that business indicators in the Third District showed mixed trends. Unemployment claims continued to decline gradually, and both new and continued claims were at the lowest levels in several years. However, seven of the 13 major labor market areas were still classified as having a substantial labor surplus. The classification of Atlantic City had been changed from "F" to "E", clearly reflecting seasonal factors; usually the change was from "E" to "D".

In view of the considerable amount of unused plant capacity and of unemployment, Mr. Bopp felt that the Committee should continue

the degree of ease that had existed thus far, with no change in the current policy directive or the discount rate.

Mr. Bryan said that the latest Sixth District figures were mostly for March, with little preliminary data for April available. These figures seemed to indicate that economic activity had edged up, although with no boom-like surge occurring. The most notable increases involved a sharp expansion of construction contract awards and a sharp rise in member bank loans. A survey of a few member banks showed that the demand for loans was increasing, with the quality of applications good.

As to the national picture, Mr. Bryan commented that the pace of expansion still appeared modest. Inflationary forces were restrained by ample plant capacity and unemployment, as well as by a mixed earnings picture and favorable investment opportunities abroad. The moderate pace of the upturn and other factors argued against a policy that would lessen the supply of bank reserves. Accordingly, there seemed no reason for an overt change in policy such as a change in the discount rate, and he would continue to supply reserves in approximately seasonal proportions, plus a modest growth factor. In April the daily average of total reserves was about $19,700 million. On the basis of a three per cent annual growth rate the daily average for May would be around $19,750 million, which would be satisfactory to him as a rough target. If this were converted to free reserves,

the target would appear to be about $425 million. In his view a 3 per cent growth rate was ample at the present time. If banks needed reserves in greater volume, those reserves could be sought through the discount window.

Mr. Francis noted that most of this year Eighth District activity seemed to have lagged behind the nation. However, recent data indicated that District figures more nearly approximated national trends. Recent conversations with a number of businessmen and others in the District seemed to support that conclusion. Almost without exception, business was said to be better than last year, and that the outlook for the immediate future was regarded as good. No concern was expressed about the possibility of a runaway type of expansion.

Mr. Balderston commented that a couple of weeks ago, on the basis of figures then available, he thought perhaps the time had come to press on the brakes. Liquid assets for March were up to an extent that produced an annual rate of increase for the first quarter of about 10 per cent. Also, the money supply, if time deposits were included, rose during the first four months of the year by about 10 per cent. However, in studying what had happened it seemed to him that funds had moved from the hands of the Treasury into private deposits in the latter part of March, and that the picture shown on the chart that the Committee had been using was in large part explained by that

movement. For the past four or five weeks required reserves against private deposits had been growing not at a 6 per cent annual rate but at only about a 4 per cent rate.

The principal question in his mind in recent weeks, Mr. Balderston said, had been whether the economy was at last moving in such fashion as to require some curbing of the rate of credit expansion. His conclusion at the moment, however, was that this was not the case. In terms of the projections referred to by Mr. Koch, it appeared that the economy might be following the low road rather than the high road. Despite such factors as near-record sales of automobiles and a sharp increase in housing starts, the economy did not yet show the same characteristics of ebullience as in 1958-59 and 1955-56. The rate of inventory accumulation was moderate, along with the rate of fixed investment. Moreover, it appeared that the stock and bond markets might be reflecting some change in inflationary expectations; something was happening in the minds of investors that made the stock market look less attractive at the moment, and foreign pastures seemed to look greener from the standpoint of investment opportunities. On the other hand, the balance-of-payments situation seemed not to have worsened in the past month, although the progress toward a basic balance might not be too encouraging. The best answer to the question of how much bank credit fed in by the Federal Reserve was seeping out to other countries might be that last year about $2 billion of bank funds were loaned to Japan and other countries, or one out of every seven dollars of bank credit provided.

Mr. Balderston said that, in coming to the conclusion that the Committee should continue its current policy without change for a while longer, he was influenced by these considerations: (1) the steel price episode had unsettled the minds of businessmen as to fixed investments, and businessmen would be watching for any action by the Federal Reserve System that would confirm their suspicions that the Government was trying to restrain profit making; (2) he was not sure that an increase in interest rates would restrain the kind of borrowing that the Japanese seemed to be doing in this country. With interest rates as high as they were in Japan, those firms would not be inhibited from borrowing in this country even if rates were much higher than at the moment. In suggesting a continuation of present monetary policy, he realized there was the risk of some day running into a real crisis due to the outflow of gold. At present, however, he saw a continued need to foster domestic expansion. On balance, therefore, he would continue present policy, with no change in the existing policy directive.

Chairman Martin expressed the view that this was a period when monetary policy could do very little more than was now being done. He agreed with Mr. Wayne's comments about the limitations of monetary policy under current circumstances. If that was correct, it seemed to him that maintenance of the status quo was about the best contribution that could be made. In his opinion, "no change, more ease" and "no change, less ease" defied definition from the standpoint of the

conduct of open market operations. While he might question some words in the current policy directive and while, if the directive were being written afresh, Mr. Shepardson's suggestion for "permitting" rather than "promoting" further credit and monetary expansion might be good phrasing, it was his feeling on the basis of the discussion at this meeting that the best course would be to retain the existing directive, thus reasserting for the next three weeks the policy that the Committee had been following. There would be another meeting of the Committee in three weeks, and the Treasury would be out of market for a while. The Committee might have at that time a better perspective of what the economy was doing. At the moment, any improvement in the economy was offset--perhaps more than offset--by uncertainties affecting business confidence. One could hardly say that there was a definite improvement in the business picture until the confidence factor had been resolved more effectively. It might be that the picture would be clearer by the time of the next meeting than it was today.

Chairman Martin then proposed that the current economic policy directive be retained and that the Committee continue its present policy for the next three weeks.

Mr. Mills stated that he would like to be recorded as voting against renewal of the existing directive for reasons that he had previously expressed.

Mr. Treiber indicated that the differences between his position

and a continuation of the policy embodied in the existing directive were not sufficient to cause him to record a dissenting vote.

There were no other comments by members of the Committee and, in response to a question, Mr. Stone indicated that he had no comment.

> Thereupon, upon motion duly made and seconded, the Federal Reserve Bank of New York was authorized and directed until otherwise directed by the Committee to effect transactions for the System Open Market Account in accordance with the following current economic policy directive:

In view of the modest nature of recent advances in the pace of economic activity and the continued underutilization of resources, it remains the current policy of the Federal Open Market Committee to promote further expansion of bank credit and the money supply, while giving recognition to the country's adverse balance of payments and the need to maintain a viable international payments system.

To implement this policy, operations for the System Open Market Account during the next three weeks shall be conducted with a view to maintaining a supply of reserves adequate for further credit and monetary expansion, taking account of the desirability of avoiding sustained downward pressures on short-term interest rates.

> Votes for this action: Messrs. Martin, Balderston, Bryan, Deming, Ellis, Fulton, King, Mitchell, Robertson, Shepardson, and Treiber. Vote against this action: Mr. Mills.

Mr. Williams then withdrew from the meeting.

There had been distributed to the Committee a report from the Special Manager of the System Open Market Account on System and Treasury operations in foreign currencies and on foreign exchange market conditions for the period April 17 through May 2, 1962, along with a supplementary report for the period May 3 through May 7, 1962. Copies of these reports have been placed in the files of the Federal Open Market Committee.

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

Since the last meeting of the Committee, on April 17, the most important development in the foreign exchange market has been the re-establishment by Canada of a par value. The new par declared to the International Monetary Fund of U. S. $0.92-1/2 = $1.00 Canadian was established well after the close of business May 2. So far as the Canadian exchange rate is concerned, the devaluation of about 3 per cent from the previous level passed off quite easily but it did have some repercussion in the Swiss franc market and in the London gold market.

In Switzerland an atmosphere of uneasiness developed. People pointed to the devaluation of the Canadian dollar and linked that with the possibility of changes occurring in one or more other currencies. The closing spot rate for the Swiss franc rose somewhat (from $.2302-1/4 on May 2 to $.2305-3/8 on May 3 and $.2307 on May 4), and in order to avoid the uneasiness from feeding on itself and perhaps spreading to other currencies, i.e., the United States dollar, the U. S. Stabilization Fund sold a total of 6-1/2 million Swiss francs on those two days. As time progressed, it became more evident that a fairly strong flow of funds to Switzerland (sources unknown) had developed and the Stabilization Fund ceased, at least temporarily, operating in the market.

The market uncertainties resulting from the Canadian rate change were reflected in an increased demand for gold in London. The dollar equivalent of the fixing price rose one cent from Wednesday's level to $35.0808 by Monday, with half this increase coming on Monday when demand was reported to be quite heavy, and today the price is up further to $35.0824.

Since the last meeting of the Committee there have been no operations in foreign exchange for System Account. On the other hand, the Stabilization Fund has had transactions in several currencies--Deutschemarks, Netherlands guilders, and Swiss francs.

The range of fluctuation of the Deutschemark has been only between $0.2499-5/8 and $0.2501. On May 1 the Bundesbank, believing that the danger of hot money flows to Germany has now lessened and that the German balance of payments is closer to equilibrium, authorized German banks to resume interest payments on nonresident time deposits. In the circumstances the Deutschemark may in the near future be more often below par than above and in fact today declined to slightly below par. Thus, an opportunity may be afforded to build up System holdings of Deutschemarks for

possible use in the future. If we should arrive at a judgment that System acquisition of Deutschemarks is desirable at the time, in consultation with Bundesbank, it would be discussed with the Committee's staff and reported to the Committee as a matter of course, as acquisitions contemplated at this time would only be made within the guidelines, which state that acquisitions should be made at or below par, in so far as practicable.

On April 24 the Nederlandsche Bank announced an increase in its discount rate to 4 per cent from 3-1/2 per cent, a step which was taken to restrain domestic inflationary pressures. This increase was not generally anticipated by the exchange market because Dutch international reserves had been rising. As traders attempted to cover commitments entered into prior to the announcement of the increase, some upward pressure was exerted on the guilder rate, and to restrain any sharp rise in the exchange rate which might have had an adverse effect on the international position of the dollar, we, acting for the Stabilization Fund, and in consultation with the Nederlandsche Bank, sold a total of 7 million guilders on April 24, 27, and 30. Our action in countering the fairly sharp slump of the dollar against the guilder exercised a braking action on the movement. It also resulted in a clearer understanding between the Nederlandsche Bank and ourselves as to cooperation, i.e., it established a clearer understanding that we can sell in the New York market. We are, of course, still appraising the effect of too rapid changes in exchange rates on public attitudes and psychology. Meanwhile, the three-month forward guilder rate has declined from a premium of 0.10 per cent per annum to a discount of 0.65 per cent.

Mr. Coombs is presently in Europe. In Basle he has, at the request of the Treasury Department, been meeting with the central bank foreign department experts on the completion of arrangements relating to the London gold market. In London he has been discussing with the British the question of a proposed dollar-pound swap between the Federal Reserve and the Bank of England. Any such swap would, of course, be submitted to the Committee for approval. There are also discussions scheduled with the Swiss concerning a reciprocal standby credit as a supplement to the arrangements entered into by other countries with the International Monetary Fund for standby credits. I understand that good progress has been made with the Dutch on the establishment of a line of credit for the U. S. Treasury to backstop forward guilder operations. (This would be carried out through the Bank for International Settlements.) Finally, I understand conversations are also scheduled with the Belgians, who may be interested in a swap arrangement.

As you know, there has been a spate of new issues of foreign securities in the United States either already consummated or in near contemplation. The New York market for foreign security issues is both broad and completely open to borrowers, unlike the situation in the European markets, which have very limited capacity and considerable official control. In the case of the Danish Government $20 million issue, we had discussed with Mr. Hartogsohn, Deputy Governor of the Danmarks Nationalbank, during his visit with us, the disposition of the proceeds of this issue and had been informed that he believed they would be transferred into sterling, which he likened to a borrowing from the Chase Bank, which is immediately checked out and deposited in the National City Bank. He, therefore, contacted his Governor and we have now been informed that the funds will remain in the United States until such time as the Danes need to disburse the funds here and in other countries. Similar discussions have occurred in the case of the New Zealand $25 million issue, which, if the past pattern is followed, would result in transfer of the proceeds to the United Kingdom dollar pool; at this moment there has been no definitive reply from the New Zealand authorities as to their decision in the case of the present issue. The significance of such borrowing and immediate conversion into sterling is that the gain of dollars to the United Kingdom results in an immediate equivalent conversion into gold obtained from the U. S. Treasury. Hence, the Treasury and we consider it desirable to arrange, if possible, for conversion into other currencies only as and when the need for such currencies may arise.

Following a brief discussion based on Mr. Sanford's comments, it was noted that inasmuch as there had been no System foreign currency transactions during the period since the Open Market Committee meeting on April 17, 1962, no action to approve, ratify, and confirm any such transactions was necessary.

All of those present except the members and alternate members of the Committee, the other Reserve Bank Presidents, Messrs. Francis, Young, Sherman, and Kenyon then withdrew from the meeting.

Pursuant to an understanding during an executive session of the meeting of the Open Market Committee on January 23, 1962, Messrs. Martin, Hayes, and Balderston had been holding informal exploratory discussions looking toward the selection of a successor to Mr. Rouse as Manager of the System Open Market Account. At the meeting on April 17, 1962, it was agreed that this group would submit a report to the Committee for consideration at a later meeting. Such a report, dated May 1, 1962, was distributed to the Committee under date of May 3, 1962. In this report the group recommended that Robert W. Stone, Assistant Vice President of the Federal Reserve Bank of New York, be selected to succeed Mr. Rouse as Manager of the Open Market Account and suggested that the appointment be made effective on a date to be agreed upon by the Committee and the New York Bank, perhaps May 15, 1962. In a letter dated May 1, 1962, to Chairman Martin, Mr. Rouse submitted his resignation as Manager of the Open Market Account.

In discussion, Chairman Martin commented that the recommendation with respect to Mr. Stone reflected both the views expressed by a number of persons outside the Federal Reserve System regarding Mr. Stone's qualifications and observation by members of the three-man group concerning Mr. Stone's work on the Desk.

Thereupon, upon motion duly made and seconded, and by unanimous vote, Mr. Rouse's resignation as Manager of the System Open Market Account was accepted as of the close

of business May 14, 1962, and Mr. Stone was selected as Manager of the System Open Market Account to succeed Mr. Rouse, effective at the beginning of business May 15, 1962, it being understood that Mr. Stone's selection was subject to his being satisfactory to the Board of Directors of the New York Reserve Bank.

Upon motion duly made and seconded, the Secretary of the Committee was requested to prepare appropriate expressions of appreciation for presentation to Mr. Rouse and to Mr. Woodlief Thomas on suitable occasions in recognition of their signal services to the Committee over many years as Manager of the System Open Market Account and as Economist of the Federal Open Market Committee, respectively.

In further discussion, Mr. Treiber said he anticipated that the directors of the New York Reserve Bank at their meeting on Thursday, May 10, would appoint Mr. Rouse as Vice President and Senior Adviser of the Bank, appoint Mr. Stone as Vice President of the Bank, and approve Mr. Stone's selection as Manager of the System Open Market Account.

As to the manner of public announcement with respect to Mr. Stone's selection as Account Manager, it was understood that this announcement would be released by the Open Market Committee along with advice of the resignation of Mr. Rouse as Account Manager. It was agreed that the timing of the announcement, and of the announcement by the New York Reserve Bank of the new officer posts at the Bank for Messrs. Rouse and Stone, would be worked out between the Bank and Mr. Molony, Assistant to the Board of Governors.

It was agreed that the next meeting of the Federal Open Market Committee would be held on Tuesday, May 29, 1962.

The meeting then adjourned.

Secretary