

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 5, 1963, at 9:30 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Hayes, Vice Chairman
Mr. Balderston
Mr. Bopp
Mr. Clay
Mr. Irons
Mr. King 1/
Mr. Mills
Mr. Mitchell
Mr. Robertson
Mr. Scanlon
Mr. Shepardson

Messrs. Fulton, Wayne, Shuford, and Swan, Alternate Members of the Federal Open Market Committee

Messrs. Ellis, Bryan, and Deming, Presidents of the Federal Reserve Banks of Boston, Atlanta, and Minneapolis, respectively

Mr. Young, Secretary
Mr. Sherman, Assistant Secretary
Mr. Kenyon, Assistant Secretary
Mr. Hackley, General Counsel
Mr. Hexter, Assistant General Counsel
Mr. Noyes, Economist
Messrs. Baughman, Brill, Eastburn, Furth, Garvy, Green, Hol'and, and Koch, Associate Economists
Mr. Stone, Manager, System Open Market Account
Mr. Coombs, Special Manager, System Open Market Account

Mr. Molony, Assistant to the Board of Governors
Mr. Farrell, Director, Division of Bank Operations, Board of Governors
Mr. Williams, Adviser, Division of Research and Statistics, Board of Governors

1/ Withdrew from meeting at point indicated in minutes

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Mr. Yager, Chief, Government Finance Section,
Division of Research and Statistics, Board
of Governors

Messrs. Ratchford, Jones, and Parsons, Vice
Presidents of the Federal Reserve Banks
of Richmond, St. Louis, and Minneapolis,
respectively

Messrs. Brandt and Lynn, Assistant Vice
Presidents of the Federal Reserve Banks
of Atlanta and San Francisco, respectively

Mr. Anderson, Financial Economist, Federal
Reserve Bank of Boston

Mr. Sternlight, Manager, Securities Department
Federal Reserve Bank of New York

Mr. Mann, Senior Economist, Federal Reserve
Bank of Cleveland

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 the term of one year commencing March 1, 1963, and that it appeared such persons would be legally qualified to serve after they had executed their oaths of office.

The elected members and alternates, all of whom had now executed their oaths of office, 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;

Karl R. Bopp, President of the Federal Reserve Bank of Philadelphia, with Edward A. Wayne, President of the Federal Reserve Bank of Richmond, as alternate;

Charles J. Scanlon, President of the Federal Reserve Bank of Chicago, with Wilbur D. Fulton, President of the Federal Reserve Bank of Cleveland, as alternate;

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George H. Clay, President of the Federal Reserve Bank of Kansas City, with Eliot J. Swan, President of the Federal Reserve Bank of San Francisco, as alternate;

Watrous H. Irons, President of the Federal Reserve Bank of Dallas, with Harry A. Shuford, President of the Federal Reserve Bank of St. Louis, as alternate.

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 29, 1964, 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
Guy E. Noyes	Economist
Ernest T. Baughman, Daniel H. Brill, David P. Eastburn, J. Herbert Furth, George Garvy, Ralph T. Green, Robert C. Holland, Albert R. Koch, and Clarence W. Tow	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 Federal Open Market Committee after February 29, 1964.

Upon motion duly made and seconded, and by unanimous vote, Robert W. Stone

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and Charles A. Coombs were selected to serve at the pleasure of the Federal Open Market Committee as Manager of the System Open Market Account and as Special Manager for foreign currency operations for such Account, respectively, it being understood that their selection was subject to their being satisfactory to the Board of Directors of the Federal Reserve Bank of New York.

Secretary's Note: Advice was subsequently received that Messrs. Stone and Coombs were satisfactory to the Board of Directors of the New York Reserve Bank for service in the respective capacities indicated.

In connection with the foregoing action, Mr. Hayes recalled that at the meeting of the Federal Open Market Committee on April 17, 1962, he and Mr. Reed, Chairman of the Federal Reserve Bank of New York, had presented arguments against the proposal, then under consideration, to change the procedure whereby the Manager and Special Manager of the System Open Market Account were selected by the Federal Reserve Bank that was selected to execute transactions for the System Account, subject to approval by the Open Market Committee. As a possible compromise, Mr. Hayes noted, he had suggested a process of joint appointment of the Manager and Special Manager by the Open Market Committee and the Reserve Bank. Considerable sympathy had been expressed with that suggestion, but in the end the Committee had voted (with Mr. Hayes dissenting) to amend its By-Laws to provide for selection by the Committee of a Manager and a Special Manager, both of whom were

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to be satisfactory to the Reserve Bank selected to execute transactions for the System Account.

That decision having been made, Mr. Hayes said, he saw no purpose in pursuing the matter further. He merely would like to make the comment for the record that although he would go along with the current procedure, he did so with some reluctance.

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meetings of the Federal Open Market Committee held on January 29 and February 12, 1963, were approved.

Consideration then was given to the continuing authorizations of the Committee, according to the customary practice of reviewing such matters at the first meeting in March of each year, and the actions set forth hereinafter were taken.

Upon motion duly made and seconded, it was voted, with Mr. Robertson abstaining, to authorize and direct the Federal Reserve Bank of New York, until otherwise directed by the Committee, to execute transactions in the System Open Market Account in accordance with the following continuing authority directive relating to transactions in U. S. Government securities and bankers' acceptances:

1. The Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York, to the extent necessary to carry out the current economic policy directive adopted at the most recent meeting of the Committee:

(a) To buy or sell United States Government securities in the open market, from or to Government securities dealers and foreign and international accounts maintained at the Federal Reserve Bank of New York, on a cash, regular, or deferred delivery basis, for the System Open Market Account at market

prices and, for such Account, to exchange maturing United States Government securities with the Treasury or allow them to mature without replacement; provided that the aggregate amount of such securities held in such Account (including forward commitments, but not including such special short-term certificates of indebtedness as may be purchased from the Treasury under paragraph 2 hereof) shall not be increased or decreased by more than \$1 billion during any period between meetings of the Committee;

(b) To buy or sell prime bankers' acceptances of the kinds designated in the Regulation of the Federal Open Market Committee in the open market, from or to acceptance dealers and foreign accounts maintained at the Federal Reserve Bank of New York, on a cash, regular, or deferred delivery basis, for the account of the Federal Reserve Bank of New York at market discount rates; provided that the aggregate amount of bankers' acceptances held at any one time shall not exceed \$75 million or 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;

(c) To buy United States Government securities with maturities of 24 months or less at the time of purchase, and prime bankers' acceptances with maturities of 6 months or less at the time of purchase, from non-bank dealers for the account of the Federal Reserve Bank of New York under agreements for repurchase of such securities or acceptances in 15 calendar days or less, at rates not less than (a) the discount rate of the Federal Reserve Bank of New York at the time such agreement is entered into, or (b) the average issuing rate on the most recent issue of 3-month Treasury bills, whichever is the lower; provided that in the event Government securities covered by any such agreement are not repurchased by the dealer pursuant to the agreement or a renewal thereof, they shall be sold in the market or transferred to the System Open Market Account; and provided further that in the event bankers' acceptances covered by any such agreement are not repurchased by the seller, they shall continue to be held by the Federal Reserve Bank or shall be sold in the open market.

2. The Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York to purchase directly from the Treasury for the account of the Federal Reserve Bank of New York (with discretion, in cases where it seems desirable, to issue participations to one or more Federal Reserve Banks) such amounts of special short-term certificates of indebtedness as may be necessary from time to time for the temporary accommodation of the Treasury; provided that the rate charged on such

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certificates shall be a rate $1/4$ of 1 per cent below the discount rate of the Federal Reserve Bank of New York at the time of such purchases; and provided further that the total amount of such certificates held at any one time by the Federal Reserve Banks shall not exceed \$500 million.

In discussion that preceded the foregoing action, which continued in effect the directive adopted by the Committee on March 6, 1962, Mr. Mills commented that he would accept the directive because its construction was susceptible of the kind of policy that he thought it was appropriate for the Committee to pursue, namely, a reversion to the practice that called for transactions in the System Account to be limited to supplying and withdrawing reserves with, except in unusual circumstances, the understanding that such transactions would be carried out through the purchase and sale of Treasury bills rather than by operations in other areas of the Government securities market. This was a reiteration, he noted, of views he had expressed on previous occasions.

Mr. Robertson said it continued to be his view that the continuing authority directive was inadequate and lacked sufficient guidance and restrictions, which view he had expressed at the meeting on March 6, 1962, and also in connection with the adoption of the continuing authority directive on December 19, 1961. In his opinion, the directive in its present form served no purpose other than as window dressing. Therefore, he would abstain from voting on the directive.

Upon motion duly made and seconded, and by unanimous vote, the Authorization Regarding Open Market Transactions in Foreign Currencies (as amended November 13, 1962) and the Guidelines for System Foreign Currency Operations (as amended November 13, 1962) were reaffirmed:

AUTHORIZATION REGARDING OPEN MARKET TRANSACTIONS IN
FOREIGN CURRENCIES

Pursuant to Section 12A of the Federal Reserve Act and in accordance with Section 214.5 of Regulation N (as amended) of the Board of Governors of the Federal Reserve System, the Federal Open Market Committee takes the following action governing open market operations incident to the opening and maintenance by the Federal Reserve Bank of New York (hereafter sometimes referred to as the New York Bank) of accounts with foreign central banks.

I. Role of Federal Reserve Bank of New York

The New York Bank shall execute all transactions pursuant to this authorization (hereafter sometimes referred to as transactions in foreign currencies) for the System Open Market Account, as defined in the Regulation of the Federal Open Market Committee.

II. Basic Purposes of Operations

The basic purposes of System operations in and holdings of foreign currencies are:

- (1) To help safeguard the value of the dollar in international exchange markets;
- (2) To aid in making the existing system of international payments more efficient and in avoiding disorderly conditions in exchange markets;
- (3) To further monetary cooperation with central banks of other countries maintaining convertible currencies, with the International Monetary Fund, and with other international payments institutions;
- (4) Together with these banks and institutions, to help moderate temporary imbalances in international payments that may adversely affect monetary reserve positions; and

- (5) In the long run, to make possible growth in the liquid assets available to international money markets in accordance with the needs of an expanding world economy.

III. Specific Aims of Operations

Within the basic purposes set forth in Section II, the transactions shall be conducted with a view to the following specific aims:

- (1) To offset or compensate, when appropriate, the effects on U. S. gold reserves or dollar liabilities of disequilibrating fluctuations in the international flow of payments to or from the United States, and especially those that are deemed to reflect temporary forces or transitional market unsettlement;
- (2) To temper and smooth out abrupt changes in spot exchange rates and moderate forward premiums and discounts judged to be disequilibrating;
- (3) To supplement international exchange arrangements such as those made through the International Monetary Fund; and
- (4) In the long run, to provide a means whereby reciprocal holdings of foreign currencies may contribute to meeting needs for international liquidity as required in terms of an expanding world economy.

IV. Arrangements with Foreign Central Banks

In making operating arrangements with foreign central banks on System holdings of foreign currencies, the New York Bank shall not commit itself to maintain any specific balance, unless authorized by the Federal Open Market Committee.

The Bank shall instruct foreign central banks regarding the investment of such holdings in excess of minimum working balances in accordance with Section 14(e) of the Federal Reserve Act.

The Bank shall consult with foreign central banks on coordination of exchange operations.

Any agreements or understandings concerning the administration of the accounts maintained by the New York Bank with the central banks designated by the Board of Governors under Section 214.5 of Regulation N (as amended) are to be referred for review and approval

to the Committee, subject to the provision of Section VIII, paragraph 1, below.

V. Authorized Currencies

The New York Bank is authorized to conduct transactions for System Account in such currencies and within the limits that the Federal Open Market Committee may from time to time specify.

VI. Methods of Acquiring and Selling Foreign Currencies

The New York Bank is authorized to purchase and sell foreign currencies in the form of cable transfers through spot or forward transactions on the open market at home and abroad, including transactions with the Stabilization Fund of the Secretary of the Treasury established by Section 10 of the Gold Reserve Act of 1934 and with foreign monetary authorities.

Unless the Bank is otherwise authorized, all transactions shall be at prevailing market rates.

VII. Participation of Federal Reserve Banks

All Federal Reserve Banks shall participate in the foreign currency operations for System Account in accordance with paragraph 3 G (1) of the Board of Governors' Statement of Procedure with Respect to Foreign Relationships of Federal Reserve Banks dated January 1, 1944.

VIII. Administrative Procedures

The Federal Open Market Committee authorizes a Subcommittee consisting of the Chairman and the Vice Chairman of the Committee and the Vice Chairman of the Board of Governors (or in the absence of the Chairman or of the Vice Chairman of the Board of Governors the members of the Board designated by the Chairman as alternates, and in the absence of the Vice Chairman of the Committee his alternate) to give instructions to the Special Manager, within the guidelines issued by the Committee, in cases in which it is necessary to reach a decision on operations before the Committee can be consulted.

All actions authorized under the preceding paragraph shall be promptly reported to the Committee.

The Committee authorizes the Chairman, and in his absence the Vice Chairman of the Committee, and in the absence of both, the Vice Chairman of the Board of Governors:

- (1) With the approval of the Committee, to enter into any needed agreement or understanding with the Secretary of the Treasury about the division of responsibility for foreign currency operations between the System and the Secretary;
- (2) To keep the Secretary of the Treasury fully advised concerning System foreign currency operations, and to consult with the Secretary on such policy matters as may relate to the Secretary's responsibilities;
- (3) From time to time, to transmit appropriate reports and information to the National Advisory Council on International Monetary and Financial Problems.

IX. Special Manager of System Open Market Account

A Special Manager of the Open Market Account for foreign currency operations shall be selected in accordance with the established procedures of the Federal Open Market Committee for the selection of the Manager of the System Open Market Account.

The Special Manager shall direct that all transactions in foreign currencies and the amounts of all holdings in each authorized foreign currency be reported daily to designated staff officials of the Committee, and shall regularly consult with the designated staff officials of the Committee on current tendencies in the flow of international payments and on current developments in foreign exchange markets.

The Special Manager and the designated staff officials of the Committee shall arrange for the prompt transmittal to the Committee of all statistical and other information relating to the transactions in and the amounts of holdings of foreign currencies for review by the Committee as to conformity with its instructions.

The Special Manager shall include in his reports to the Committee a statement of bank balances and investments payable in foreign currencies, a statement of net profit or loss on transactions to date, and a summary of outstanding unmatured contracts in foreign currencies.

X. Transmittal of Information to Treasury Department

The staff officials of the Federal Open Market Committee shall transmit all pertinent information on System foreign currency transactions to designated officials of the Treasury Department.

XI. Amendment of Authorization

The Federal Open Market Committee may at any time amend or rescind this authorization.

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GUIDELINES FOR SYSTEM FOREIGN CURRENCY OPERATIONS

1. Holdings of Foreign Currencies

Until otherwise authorized, the System will limit its holdings of foreign currencies to that amount necessary to enable its operations to exert a market influence. Holdings of larger amounts will be authorized only when the U. S. balance of international payments attains a sufficient surplus to permit the ready accumulation of holdings of major convertible currencies.

Holdings of a currency shall generally be kept sufficient to meet forward contracts in that currency (exclusive of contracts made under parallel arrangements with foreign monetary authorities which provide their own cover) expected to mature in the following three-week period.

Foreign currency holdings above a certain minimum shall be invested as far as practicable in conformity with Section 14(e) of the Federal Reserve Act.

2. Exchange Transactions

System exchange transactions shall be geared to pressures of payments flows so as to cushion or moderate disequilibrating movements of funds and their destabilizing effects on U. S. and foreign official reserves and on exchange markets.

In general, these transactions shall be geared to pressures connected with movements that are expected to be reversed in the foreseeable future; when expressly authorized by the Federal Open Market Committee, they may also be geared on a short-term basis to pressures connected with other movements.

Subject to express authorization of the Committee, the Federal Reserve Bank of New York may enter into reciprocal arrangements with foreign central banks on exchange transactions ("swap" arrangements), which arrangements may be wholly or in part on a standby basis.

The New York Bank shall, as a usual practice, purchase and sell authorized currencies at prevailing market rates without trying to establish rates that appear to be out of line with underlying market forces.

If market offers to sell or buy intensify as System holdings increase or decline, this shall be regarded as a clear signal for a review of the System's evaluation of international payments flows. This review might suggest a temporary change in System holdings of a particular convertible currency and possibly direct exchange transactions with the foreign central bank involved to be able to accommodate a larger demand or supply.

Starting operations at a time when the United States is not experiencing a net inflow of any eligible foreign currency may require that initial System holdings (apart from sums that might be acquired from the Stabilization Fund) be purchased directly from foreign central banks.

It shall be the practice to arrange with foreign central banks for the coordination of foreign currency transactions in order that System transactions do not conflict with those being undertaken by foreign monetary authorities.

3. Transactions in Spot Exchange

The guiding principle for transactions in spot exchange shall be that, in general, market movements in exchange rates, within the limits established in the International Monetary Fund Agreement or by central bank practices, index affirmatively the interaction of underlying economic forces and thus serve as efficient guides to current financial decisions, private and public.

Temporary or transitional fluctuations in payments flows may be cushioned or moderated whenever they occasion market anxieties, or undesirable speculative activity in foreign exchange transactions, or excessive leads and lags in international payments.

Special factors making for exchange market instabilities include (i) responses to short-run increases in international political tension, (ii) differences in phasing of international economic activity that give rise to unusually large interest rate differentials between major markets, or (iii) market rumors of a character likely to stimulate speculative transactions.

Whenever exchange market instability threatens to produce disorderly conditions, System transactions are appropriate if the Special Manager, in consultation with the Federal Open Market Committee, or in an emergency with the members of the Committee designated for that purpose, reaches a judgment that they may help to re-establish supply and demand balance at a level more consistent with the prevailing flow of underlying payments. Whenever supply or demand persists in influencing exchange rates in one direction, System transactions should be modified, curtailed, or eventually discontinued pending a re-assessment by the Committee of supply and demand forces.

4. Transactions in Forward Exchange

Occasion to engage in forward transactions will arise mainly when forward premiums or discounts are inconsistent with interest rate differentials and are giving rise to a disequilibrating movement of short-term funds, or when it is deemed appropriate to supplement existing market facilities for forward cover as a means of encouraging the retention or accumulation of dollar holdings abroad.

Proposals of the Special Manager to initiate forward operations shall be submitted to the Committee for advance approval.

For such operations, the New York Bank may, where authorized, take over from the Stabilization Fund outstanding contracts for forward sales or purchases of authorized currencies.

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5. Exchange Rates

Insofar as practicable, the New York Bank shall purchase a currency through spot transactions at or below its par value, and should lower the rate at which it is prepared to purchase a currency as its holdings of that currency approach the established maximum.

The Bank shall also, where practicable, sell a currency through spot transactions at rates at or above its par value, and should raise the rate at which it is prepared to sell a currency as its holdings of that currency approach zero.

Spot transactions at rates other than those set forth in the preceding paragraphs shall be specially authorized by the members of the Committee designated in Section VIII of the Authorization for Open Market Transactions in Foreign Currencies.

In discussion preceding the foregoing action, Mr. Mills stated that he accepted the Authorization and the Guidelines on the theory that they envisaged continued experimentation with System foreign currency operations, an experiment that in his judgment had not proven completely successful in accomplishing its intended objectives. He was apprehensive about the difficulties that, according to press reports, were being encountered by U. S. authorities in financial negotiations with other countries. These reports served to heighten his feeling of apprehension with regard to the whole approach currently being followed, which he thought in a matter of time was likely to find the U. S. becoming a handmaiden of assistance to a number of its foreign allies rather than in their providing a first line of defense in time of difficulty.

Mr. Robertson stated that he concurred in the views expressed by Mr. Mills. His favorable vote on reaffirmation of the Authorization

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and Guidelines also was based on an understanding that the action contemplated a continuation of experimental operations; in other words, that the authorization for further foreign currency operations was regarded as merely a vehicle with which to carry on experimentation.

Chairman Martin commented that he thought it was generally accepted that the program of System operations in foreign currencies was of an experimental nature. Mr. Mitchell noted that this understanding had been reflected in the minutes of the Open Market Committee when the program was instituted; he suggested that it would seem desirable for this understanding also to be reflected in the minutes in connection with the current action reaffirming the Authorization and Guidelines. Mr. Hayes commented that he could not conceive that anyone would be unwilling to make such changes in the program as might appear at any time to be appropriate.

There followed a discussion during which reference was made to provisions in the Guidelines indicating that System foreign currency operations would be directed toward dealing with exchange market instabilities that might be expected to be of a temporary nature rather than fundamental disequilibria. In this connection, Mr. Hayes remarked that the limited use of foreign currencies under swap arrangements afforded an indication of the character of System operations.

Chairman Martin called attention to a second article on Treasury and Federal Reserve foreign exchange operations that had been

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prepared by the Special Manager of the Open Market Account with a view to publication in the March issues of the Federal Reserve Bulletin and the Monthly Review of the Federal Reserve Bank of New York. This article, which was of a factual nature, would bring up to date the information contained in the previous article, which had been published in September 1962. Chairman Martin commended the article to the members of the Committee for study, adding that the System program of foreign exchange operations should continue to be reviewed carefully.

There had been distributed under date of February 26, 1963, a memorandum from Messrs. Stone and Farrell submitting for consideration suggested revisions in the procedures with respect to allocations of the System Open Market Account. It was noted that on January 29, 1963, the Committee had amended such procedures so that adjustments of a Reserve Bank's holdings because of a low reserve ratio would not be made until the Bank's reserve ratio fell below 28 per cent. It had been mentioned at that time that informal staff groups from the Board of Governors and New York Reserve Bank would make a further review of the procedures. The draft of proposed procedures submitted with the February 26 memorandum incorporated changes recommended by the staff groups, in which recommendations Messrs. Stone and Farrell concurred. It was felt that adoption of the proposed changes would help to prevent the reserve ratios of individual Reserve Banks from falling

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to undesirably low levels, would reduce further the frequency of interim adjustments in holdings of System Account securities, and would also reduce the need for frequent adjustments between pledged and unpledged gold certificates in order to maintain a 25 per cent reserve against Federal Reserve notes and a 25 per cent reserve against deposits.

The principal proposed changes were as follows: (1) monthly reallocations in lieu of quarterly reallocations; (2) insertion of language that would make the raising of a Bank's reserve ratio all the way to the System average, in the course of a special adjustment, discretionary rather than mandatory; (3) elimination of the provision concerning reversal of any adjustments made in a Bank's holdings between reallocations; (4) insertion of a provision in the procedures that would give an additional participation to Banks having a relatively high proportion of note liabilities to total note and deposit liabilities; and (5) insertion of a provision that would permit allocating a Bank's participation in purchases on any one day to other Banks if it were anticipated that the Bank could not assume its participation in such purchases without incurring a reserve deficiency.

In supplementation of the memorandum, Mr. Stone made the following statement:

The proposals before the Committee grew out of the work of the two informal groups that were recently constituted within the Board and the New York Reserve Bank. I think all of us who have been involved in these discussions would agree that while

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the present proposals would carry us some distance further than the procedures now in effect, the useful life of the proposals would be rather limited if reserve ratios continue to decline. For this reason, the informal groups are continuing their work in an effort to devise procedures that would be adequate to circumstances in which reserve ratios push still closer to 25 per cent. If and when the ratios get to that point, of course, the publication of a figure below 25 per cent will be unavoidable.

I think I need comment upon only one specific point in the present proposals. That concerns the suggestion that the raising of a Bank's reserve ratio all the way to the System average during a special adjustment be made discretionary rather than mandatory. In the exercise of such discretion by the Manager and the Bank concerned, it would be my suggestion to the Bank that we go all the way to the System average if that could be done without stripping the Bank of most or all of its unpledged securities. If that could not be done, I would suggest to the Bank that, if otherwise feasible, we raise its reserve ratio as far as possible consistent with leaving some amount of unpledged securities with the Bank and available for sale in case we had to absorb reserves over the following day or two.

No question was raised, during a discussion of the matter, regarding the statement of proposed amended procedures. However, there was some discussion of a statement in the transmittal memorandum which indicated that the fourth principal proposed change, as cited heretofore, would have the effect of making additional gold certificates available as reserve against deposits. (It was subsequently clarified that the intent of this statement was to say that the change in procedure would have the effect of making additional gold certificates available "to other Banks" as reserve against deposits.)

Thereupon, upon motion duly made and seconded, and by unanimous vote, the amended procedures with respect to allocations of the System Open Market Account

were approved, effective immediately. The procedures read as follows:

1. Securities in the System Open Market Account shall be reallocated on the first business day of each month by means of adjustments proportionate to the adjustments that would have been required to equalize the average reserve ratios of the 12 Federal Reserve Banks over the first 23 days of the preceding month; provided, that the participation of each Bank, after such reallocation, shall not be less than 80 per cent of its outstanding Federal Reserve notes unless a smaller participation is necessary in order to prevent its reserve ratio from being less than 28 per cent. Any additional allocation required by the foregoing proviso shall be taken from the participations of the Banks having participations in excess of their outstanding notes, in proportion to such excesses.

2. If a Bank's reserve ratio should fall below 28 per cent on the next to the last business day (as observed by the Agent Bank) of a statement week or month, its holdings as of the close of business that day shall be adjusted by an amount sufficient to raise its reserve ratio to the average reserve ratio of the 12 Banks combined on the preceding day, or to such point as the Manager of the System Account and the Bank concerned consider feasible. Such securities shall be allocated to the Bank in a position to absorb the largest additional amount without reducing its reserve ratio below the ratio of the 12 Banks combined. If that Bank is unable to take the entire amount, the excess shall be allocated to the Bank which can absorb the next largest amount without reducing its reserve ratio below the average for the System.

3. If a Bank's reserve ratio should fall below 28 per cent on any other day, or if a Bank anticipates that its reserve ratio will fall below that figure, it may arrange with the Manager of the System Open Market Account for an adjustment similar to those provided for in paragraph 2 so as to increase the Bank's reserve ratio in any degree desired up to the average of the 12 Banks combined.

4. If purchases by the System Open Market Account on a particular day would, in the opinion of a Reserve Bank, be likely to reduce the ratio of that Bank's gold certificate reserves to its note and deposit liabilities, either combined or separately, below 25 per cent, the entire purchase shall

be allocated to other Banks. Such allocation, having the effect of a special adjustment increasing the participations of the other Banks above normal proportions, shall be made to those Banks having the largest amounts of excess gold certificate reserves in relation to total note and deposit liabilities.

5. The Account shall be apportioned during the ensuing month on the basis of the ratios determined in paragraph 1, after allowing for any adjustments as provided for in paragraphs 2, 3, and 4.

6. Profits and losses on the sale of securities from the Account shall be allocated on the day of delivery of the securities sold on the basis of each Bank's current holdings at the opening of business on that day.

Messrs. Hexter and Farrell withdrew from the meeting at this point.

The authorization for distribution of periodic reports prepared by the Federal Reserve Bank of New York for the Federal Open Market Committee, as amended March 6, 1962, was presented for consideration and certain suggested changes were mentioned.

Thereupon, upon motion duly made and seconded, and by unanimous vote, authorization was given for the following distribution:

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 and the Under Secretary of the Treasury.
- *5. The Under Secretary of the Treasury for Monetary Affairs and the Deputy Under Secretary 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.

* 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 Vice President and Senior Adviser of the Federal Reserve Bank of New York; the Assistant Vice Presidents 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 Vice President of the Foreign Function having supervisory responsibility for operations; the Senior Foreign Exchange Officer of the Foreign Function; the Managers of the Foreign Department; the officer in charge and Assistant Vice President of the Research Department of the New York Bank; the confidential files of the New York Bank as the Bank selected to execute transactions for the Federal Open Market Committee; and the Chief Federal Reserve Examiner or members of his staff.
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.

The Committee reaffirmed by unanimous vote the authorization, first given on March 1, 1951, for the Chairman to appoint a Federal Reserve Bank to operate the System Open Market Account temporarily in case the Federal Reserve Bank of New York is unable to function.

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 Interim 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.

The following resolution authorizing certain actions by the Federal Reserve Banks during an emergency was reaffirmed by unanimous vote:

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, first given at the meeting on December 16, 1958, 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 should be taken to change the existing procedure, as called for by 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.

Reference was made to the procedure authorized at the meeting of the Committee on March 2, 1955, and most recently reaffirmed on March 6, 1962, 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

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with the approval of a member of the Committee or another Reserve Bank President, with notice to the Secretary.

It was stated that lists of currently authorized persons at the Board and at each Federal Reserve Bank (excluding secretaries and records and duplicating personnel) had recently been confirmed by the Secretary of the Committee. The current lists were reported to be in the custody of the Secretary, and it was noted that revisions could be sent to the Secretary at any time.

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

This concluded the consideration of the continuing authorizations of the Open Market Committee, and the Committee turned to a review of operations during the period since the meeting of the Committee on February 12, 1963.

Before this meeting there had been distributed to the members of the Committee a report from the Manager of the System Open Market Account on operations in U. S. Government securities and bankers' acceptances during the period February 12 through February 27, 1963, and a supplemental report covering the period February 28 through March 4, 1963. 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 highlight of the recent period has been the successful advance refunding of eight issues maturing out to 1966 into four new or reopened issues maturing from 1967 to 1980. In this unusually large and rather complex operation--involving a potential exchange of about \$29 billion of outstanding issues, with public holdings amounting to about \$20 billion--the market has given a particularly good account of itself. Preliminary results, which we understand the Treasury is announcing this morning, point to an exchange of almost \$8 billion of the eligible issues, including about \$325 million exchanged by various Government trust fund accounts. Exchanges into each of the longer issues were more than \$1 billion.

The broad scope of the exchange encouraged an extraordinarily large volume of market activity, particularly in the rights and new issues directly involved in the exchange, but also in a variety of other securities. In part, this arose as investors took advantage of the opportunities for switching out of rights and moving into bills or doing their own refunding in the market. In addition, there were many reports of investors in various outstanding issues switching into the securities newly offered in the exchange. In short, the exchange was a massive catalyst opening the way to an enormous variety of portfolio adjustments. Trading volume in the Government securities market, which typically averages \$1-1/2 to \$2 billion a day, soared to \$3 - \$3-1/2 billion from February 21 (the day after the Treasury's announcement) through February 28 (the day the subscription books closed for all but individual investors). On each of the three days from February 26 to 28, market trading in rights and when-issued securities alone exceeded \$1.5 billion--which was far more than in any previous advance refunding. Indeed, the volume of trading in coupon-bearing issues on those days--which took place against a background of relatively narrow price movements--may well have been a record.

On the whole, the market atmosphere surrounding the exchange has been favorable. It has been less enthusiastic than on some past occasions when prices actually strengthened in the face of enlarged supplies of longer term issues, but there has been an undertone of dealer and investor confidence in the market. As of March 1, the net dealer position in the four new or reopened issues was about \$800 million. This was a sizable amount, but it did not appear to be too different from professional holdings at comparable dates in earlier advance refundings or regular refundings.

Subscription books for the advance refunding remain open for individual subscribers through March 8, and delivery of the new securities is to take place March 15. With that, the Treasury will have completed the second part of the three-stage program it outlined last January 30. The third stage is to be an auction of long-term bonds, now tentatively scheduled for early April. In the meantime, the Treasury is also planning to announce, later this week, the auction on March 14 of another \$1 to \$1-1/2 billion of June tax anticipation bills. Near-term financing plans also include an enlargement of the weekly bill offerings by \$100 million for a total of eight weeks starting March 28, and the addition of \$500 million to the offering of one-year bills to be sold April 15 by replacing a \$2 billion maturity with a new issue of \$2.5 billion.

Turning to System operations and money market developments, there is little to say in addition to the reports already distributed. System operations during the recent interval helped to preserve a steady money market tone in which Federal funds traded quite consistently at 3 per cent and member bank borrowing hovered around \$140 million. Treasury bill rates tended slightly lower over the period, as outright market demand was augmented to some extent by demand that stemmed from switches out of rights to the refunding. With additional market supplies of bills in prospect as a result of the Treasury financing plans noted above, and with quarterly corporate liquidity needs now drawing close, it would ordinarily be expected that bill rates would not move much lower and indeed might tend upward over the period ahead. On the other hand, these influences may be offset, in whole or in part, by downward rate pressures flowing from the reduction of the supply of short-term securities as a result of the refunding. What the net of these influences will be remains to be seen.

Chairman Martin commented that it should be borne in mind that the advance refunding, which was highly successful, had removed roughly \$6 billion of securities from the short-term area. This came at a time when the Treasury was experiencing difficulty in obtaining an extension of the present temporary debt ceiling; it now looked as

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though Congressional action was likely to be deferred until after Easter. This meant that the Treasury would be running close to the debt ceiling during the period immediately ahead, and a responsibility was placed on the Federal Reserve System to try to keep market conditions as steady as possible during this period.

With further reference to the advance refunding, the Chairman noted that most people had felt the results would be quite good if \$4 billion of securities were refunded; actually the figure was close to twice that amount. He had not felt that the 3-7/8s of 1974 would be at all popular, but they had been taken to the extent of over \$1 billion. The importance of the changes that had occurred by virtue of the advance refunding should not be underestimated.

Thereupon, upon motion duly made and seconded, the transactions in U. S. Government securities and bankers' acceptances during the period February 12 through March 4, 1963, were approved, ratified, and confirmed.

Before this meeting there had been distributed to the Committee a report from the Special Manager of the System Open Market Account on foreign exchange market conditions and on System Account and Treasury operations in foreign currencies for the period February 12 through February 27, 1963, together with a supplementary report covering the period February 28 through March 4, 1963. Copies of these reports have been placed in the files of the Committee.

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In comments supplementing the written reports, Mr. Coombs reviewed recent and prospective changes in the U. S. gold stock, summarized developments in the London gold market, and described the results of operations of the gold pool during the month of February.

Mr. Coombs then discussed recent exchange rate developments, with particular reference to the Canadian dollar and the French franc, and noted that the enlarged Federal Reserve-Bank of France swap arrangement in the amount of \$100 million became effective March 4, 1963. In that connection, he referred to certain adverse articles in the French press, apparently growing out of an erroneous interpretation along lines that the U. S. was in the process, through negotiation of the enlarged swap arrangement, of trying to borrow \$100 million from the French Government. An official of the Bank of France had called yesterday to express his regrets concerning the press articles and to assure that the enlargement of the swap arrangement was thought of as providing evidence of continuing cooperation between French and U. S. financial authorities.

Mr. Coombs went on to review recent developments with respect to the pound sterling, which had been at times under substantial pressure. He continued to be hopeful that an enlarged Federal Reserve-Bank of England swap arrangement, the negotiation of which had been authorized by the Open Market Committee, might be concluded at a relatively early date.

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Thereupon, upon motion duly made and seconded, and by unanimous vote, the System Open Market Account transactions in foreign currencies during the period February 12 through March 4, 1963, were approved, ratified, and confirmed.

Mr. Coombs pointed out that the existing \$50 million swap arrangement with the Netherlands Bank would mature March 13, 1963, and that the \$250 million swap arrangement with the Bank of Canada would mature March 26, 1963. He recommended renewal in each case for a period of three months on a stand-by basis.

Renewal of the swap arrangements with the Netherlands Bank and the Bank of Canada, as recommended by Mr. Coombs, was authorized.

Mr. Coombs then referred to a memorandum dated February 25, 1963, in which he had requested, for reasons stated, authority to undertake forward purchases in any or all of the currencies authorized for System operations up to a combined total of \$25 million equivalent for the purpose of allowing greater flexibility in covering commitments under swap arrangements. The memorandum pointed out that the Committee's Guidelines for System Foreign Currency Operations provided that the Special Manager was to submit to the Committee, for advance approval, proposals to initiate forward operations. (Mr. Coombs had mentioned this matter at the meeting of the Committee on February 12, 1963, at which time it was understood that a decision would be deferred pending the availability of a memorandum on the subject.)

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In comments supplementing the memorandum, Mr. Coombs stated that in another memorandum he would hope to put forward the case for a similar authorization covering forward sales. The present request, however, extended only to forward purchases, on an experimental basis, up to a maximum of \$25 million.

In reply to questions, Mr. Coombs reiterated that the requested authorization contemplated that any forward purchases would be limited to covering commitments under swap arrangements. He would not contemplate, without coming back to the Committee, buying forward to augment outright holdings of foreign currencies. The request envisaged experimental operations; if they worked well, possibly he might suggest at a later date an expansion of the authorization to provide for acquiring outright currency holdings through buying forward. At present, though, he was seeking authorization only to cover outstanding short positions in foreign currencies by purchasing these currencies forward. When the System drew on a swap, he noted, it was short of that particular currency and had to buy it back. This was the nature of a swap deal. While the System could buy the currency back at maturity date of the swap, it could also buy the currency back earlier, and on occasion there might be advantageous opportunities to buy forward. He felt confident that it would be possible to keep Federal Reserve forward operations of this kind distinguished clearly from forward operations of the Treasury.

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In reply to further questions, Mr. Coombs said that the \$25 million figure had been selected on an arbitrary basis. It was intended to be modest. He had assumed that Committee members might have some qualms about forward operations and that the Committee would like to have early opportunities for review. On certain occasions the total short position of the System under swap arrangements had been much greater than \$25 million. However, it would require a particular set of circumstances in which the foreign currencies were at a discount to make forward operations advantageous. Therefore, he did not anticipate extensive use of the requested authorization, but at the same time he felt that it would be a useful authorization to have available. It might save money and contribute to more efficient foreign currency operations. If it should develop that a number of useful opportunities for forward purchases presented themselves over a period of time, he could envisage the possibility of requesting that the \$25 million limit be raised to, say, \$50 million or \$75 million. He recognized that the important issue involved was not the cost of foreign currency operations to the Federal Reserve System; that was incidental and not the objective. Aside from this, however, he felt that on certain occasions it might be easier and more prudent to operate in the forward market than the spot market. It seemed important, therefore, to acquire some experience with forward operations. If they were carried out on a small scale, the risk would be minimal, and the experience should be helpful.

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Mr. Robertson stated that he regarded this as a questionable tinkering with market forces. However, in view of the very limited scope of the requested authorization, and since the authorization was requested on an experimental basis, he would approve the experimentation on this small scale. Limited operations over a period of time would tend to indicate whether his qualms were justified.

Reference was made to the provision of the Committee's continuing authority directive for foreign currency operations limiting to \$1.3 billion the holdings of foreign currencies at any one time, and question was raised as to the sufficiency of the limitation. Mr. Coombs stated that he would consider this limitation as providing adequate margin for the time being, even if the requested authorization for forward purchases should be granted. The limitation would become inadequate only in the event that certain existing swap arrangements were enlarged or new swap arrangements were concluded. In that connection Mr. Coombs referred to certain swap possibilities that might develop.

In reply to a further question, Mr. Coombs commented that the Federal Reserve System had always consulted closely with the foreign central banks concerned in undertaking any foreign currency operations. This procedure of close consultation would also be followed insofar as forward operations were concerned.

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Thereupon, upon motion duly made and seconded, and by unanimous vote, the following continuing authority directive to the Federal Reserve Bank of New York with respect to foreign currency operations was approved, effective immediately:

The Federal Reserve Bank of New York is authorized and directed to purchase and sell through spot transactions any or all of the following currencies in accordance with the Guidelines on System Foreign Currency Operations reaffirmed by the Federal Open Market Committee on March 5, 1963:

Pounds sterling
French francs
German marks
Italian lire
Netherlands guilders
Swiss francs
Belgian francs
Canadian dollars
Austrian schillings
Swedish kronor

The Federal Reserve Bank of New York is also authorized and directed to purchase, in accordance with the Guidelines and for the purpose of allowing greater flexibility in covering commitments under reciprocal currency agreements, any or all of the foregoing currencies through forward transactions, up to a combined total of \$25 million equivalent.

Total foreign currencies held at any one time shall not exceed \$1.3 billion.

This concluded the discussion of System foreign currency operations and related matters. Accordingly, the Chairman called for presentation of the usual staff economic and financial reports, and Mr. Noyes presented the following statement on economic developments:

We are always harassed at this time of the year by relatively large month-to-month changes in our basic data

that reflect normal seasonal swings rather than a fundamental change in the tempo of economic activity. This year there were 1.5 million fewer people actually employed in January than in December. Actual production at factories and mines declined almost 3 per cent from November to December, and then rose a little from December to January. Retail trade declined one-fourth from December to January. Yet in each of these cases we have observed that there was no significant change after allowance for seasonal factors.

There is no way of "correcting" data precisely for seasonal variation. No matter how complex the methodology employed, it must be based on the assumption that the seasonal influence in the current year is an extension of the seasonal pattern observed in past years. This is not a bad assumption, but neither is it a perfect one. Many seasonal influences--the weather being a good example--vary from year to year as to intensity and timing, so that previous behavior provides at best only an approximation of the month-to-month seasonal change.

The possibilities of sizable month-to-month changes that are in fact the result of seasonal influence appearing in seasonally adjusted data are obviously greatest in those months where seasonal influences are largest and, for most series, these fall on each side of the year end. No matter how skillfully and carefully the processing of the data to adjust for seasonal influence is carried out, we shall always have to exercise special care in evaluating the significance of changes that appear in this season.

But these difficulties, real as they are, certainly do not entitle us to take a four-month leave of absence each winter from our scrutiny of economic developments. We have no assurance that significant changes will not occur in this period--in fact, we know from hindsight that they sometimes have.

Our underlying statistics are essentially the facts on the performance of the economy--how many people were at work, how many tons of steel were produced, how many houses were started, and how many dollars of bank credit were actually extended. Our knowledge of these underlying facts is just as accurate in January and February as it is in any other month. It is simply a little harder to tell whether the changes that the facts reveal are transitory or are of longer range significance.

I apologize if it seems to you that I have labored this point unduly, but it is relevant to my observations as to the

present state of the economy. Despite the wide swings that have occurred in the raw data, I think it can be said with reasonable confidence that there has been no significant improvement or deterioration in over-all economic activity since November.

The percentage of the labor force unemployed has crept up a little. The February figure, due to be released on Thursday, will probably show some further increase--back to the 6 per cent level. In more concrete terms, there were 300,000 more people unemployed in February this year than there were a year ago.

We really have no sound basis for estimating industrial production in February as yet, but my own guess is that it will not change much, either way.

We do have some basis for saying that there was probably not much change in retail sales--the chances seem to favor a small decline, if anything. The performance of retail sales in January and February might be regarded as especially disappointing in view of the substantial addition to personal income in January brought about by the accelerated payment of VA insurance dividends. Some other figures--notably new orders--were up, and some were down. A rather sizable decline in the stock market appears to have been interrupted by a 7-point rise in the Dow-Jones industrial average yesterday.

But, taken altogether, it does seem to me that a fairly clear picture of horizontal movement emerges from a careful analysis of the rather wide fluctuations in the raw data on economic activity in the last three months.

Unfortunately, one of the most significant bits of forward-looking data--the Commerce-SEC survey of plant and equipment expenditure plans--will not be available for a week or so. We have, however, had a chance to look at the NICB capital appropriations survey, due for publication next week, and it suggests possible improvement in the outlook for business investment as compared to the rather discouraging picture shown by last fall's McGraw-Hill survey. This, by itself, is certainly not a sufficient basis for assuming that we will have a vigorous pick-up. It does offset to some extent, however, the rather pessimistic view one might derive from the behavior of the so-called leading indicators.

I can assure you that I am as tired of saying it as you are of hearing it, but I find myself again unable to avoid the conclusion that there not only has not been much change in the economy, on balance, since the last meeting, but that no very convincing signs have come to light to indicate the direction the next move will take when it comes.

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Mr. Brill presented the following statement on financial developments:

Many economists were puzzled, last fall and early winter, by a growing disparity in the behavior of measures of productive activity on the one hand and measures of financial activity on the other. While the production index was clinging to a plateau, the unemployment rate was bobbling in a very narrow but high range, and the average work week in manufacturing was slipping, credit demands seemed exceptionally strong and rising. In fact, our preliminary flow-of-funds measures indicate a record for the total of borrowing by Governments, consumers, and businesses in the fourth quarter of the year.

The banking system contributed substantially to this record financing volume. Bank credit rose by over \$10 billion from August through December, and more than a third of the rise was in business and consumer loans. Reflecting the continued large inflow of savings deposits, another third of the increase went to real estate loans and municipal securities. There was a substantial rise in bank financing of security dealers, but banks' own portfolios of Governments were reduced somewhat. All in all, it was a pace and pattern of bank credit growth that in the past has been typical of vigorous economic expansion periods and the beginning of monetary restraint, rather than of very mild growth and relative monetary ease.

Since the year end, however, there seems to be less incongruity between developments in credit markets and measures of economic activity. Productive activity has remained on a plateau, and unemployment has edged up. While bank credit has continued to expand--perhaps even more sharply last month than at any time last fall--it has been responding more to Government financing demands and to savings inflows, and less to any burgeoning of private credit needs. Bank purchases of Government securities and loans to dealers accounted for fully half of the bank credit expansion in January and February. Continued growth in savings inflows has been reflected in continued growth in real estate loans and municipal security holdings, but combined business and consumer lending has fallen to only a sixth of the total. The drop has been all in business loans, which hardly increased in either January or February. With the Government locking up some of the borrowing proceeds in its own cash balances, and time and savings deposits still rising, the privately held money supply showed no further growth

from January to February and required reserves against private deposits have slipped further down toward the 3 per cent guideline.

Obviously, two months' data does not make a cyclical phase, particularly these two winter months. Nevertheless, the marked drop-off in business loan demands, the relatively light current and prospective business demands for longer term funds, and--up to yesterday--an apparent pause in the rise of stock prices suggest that we may now be in a period when financial developments will more closely mirror the lack-luster performance in production and sales.

Consequences for the interest rate structure could be troublesome. Treasury needs for new money are not expected to be large over the balance of this fiscal year, and in the absence of supplementary demands from the private sectors, and with savings flows continuing large, we may once again be addressing ourselves to the problem of propping the rate structure for international capital flow purposes, but in the context of a 6 per cent unemployment rate.

There are, of course, some possibilities of a resurgence in activity that might be reflected in financial markets. As Mr. Noyes has pointed out, in a few days we will be getting a new reading on business plans for capital spending this year. The last surveys on this subject were not optimistic, but a rapid turnaround in business sentiment is not unprecedented. Back in 1956, the March Commerce survey indicated much stronger business spending plans than had been reported in the previous fall's McGraw-Hill survey, and touched off a scramble for capital market funds that resulted in a very rapid rise in long-term interest rates. With widespread expectations of a large Federal deficit and cash borrowing ahead--tax cut or no--a bullish report by the Department of Commerce this month could touch off such a scramble again.

In the short-term area, General Motors' very publicly announced intention to stockpile steel against strike possibilities might spark an upsurge in business loan demands generally, and there doesn't seem to be any evidence foreshadowing a slackening in consumer demands for new cars or for the credit to finance these car purchases.

Such developments could provide an underpinning for the current rate structure, but in their absence it is hard to see what demand forces in the spring months would overcome the depressing influence on rates of a continued very large volume of savings. Perhaps once again it may be necessary to depend on the Treasury to borrow and build up its cash

balances in order to maintain the current level of short rates. The Treasury will first have to persuade Congress to raise the debt ceiling, however. The present ceiling leaves some margin over actual cash needs this month, but becomes very restrictive on April 1.

Over the very short term, market forces will likely operate to keep rates up for a while. We may already have had a large share of the adjustment in short-term rates likely to stem from the Treasury's refunding, with "rights" switching by dealers, corporations, and institutions largely completed by the end of last week. Until about midmonth, corporate needs for cash to make tax and dividend payments and dealer needs to finance "rights" will help maintain money market pressures. After midmonth, however, these pressures should moderate.

Present and still tentative Treasury financing plans would replace the \$3 billion March tax bill maturing on March 22 with a June tax bill of \$1-1/2 billion paid in on that date, plus an increase in the weekly bill auctions beginning March 25 and an increase in the one-year bill in mid-April. Whether the contemplated amount and timing of Treasury offerings will be enough to sustain rate levels--after the switch out of about \$6 billion of short-term instruments in the refunding and in the face of high corporate cash flows and reinvestment demands stemming from the fairly large municipal calendar--is a matter of fine judgment. The situation developing later in the month--around the week beginning March 20--could be one of renewed downward pressure on short rates. Moreover, this is the period in which the demand for short bills generated by the April 1 Cook County property tax reaches a maximum.

Mr. Furth presented the following statement with respect to the

U. S. balance of payments:

Net transfers of gold, dollars, and other convertible currencies to foreigners during February are tentatively estimated at \$100-\$150 million, less than half the January figure. In view of the effects of the dock strike, however, the January and February figures should be combined; this gives a monthly average of perhaps \$250 million--only slightly lower than the monthly average for 1962. The gold portion of these transfers, about \$80 million a month, was slightly higher than the monthly average for 1962.

The January-February average is consistent with recent projections of the deficit for 1963. Deducting expected

further prepayments of European debts to the U. S. Government, the payments deficit for 1963 might be guessed at about \$2-1/2 billion. Although this actually would be a modest improvement over 1962, the statistical adjustments made last year would give the impression of a deterioration, with possible repercussions in international financial markets.

Even without such repercussions, the problem of covering such a deficit by means other than gold will be difficult to solve. If the foreign payments surpluses that must correspond to the U. S. deficit were to accrue to Canada or to less developed nations, we could count on these countries increasing their holdings of U. S. dollars. But if the surpluses were again to be concentrated in Continental Europe, we should be confronted with a decided unwillingness of these nations to cooperate in protecting our gold reserves, except perhaps by very temporary means such as System swaps--means that should be preserved for an emergency and not be used to finance a persistent deficit.

In this connection, it is intriguing to find that virtually all Continental European nations project a decline in their payments surplus for 1963. Unfortunately, similar projections for earlier years have generally proven to be exaggerated. This year they sound slightly less unrealistic, in view of the continuing rise in European costs and prices and in view of the uncertainties about the continuation of the flow of U. S. capital to Europe created by the recent Common Market difficulties. Should these projections for once turn out to be correct, the international financial position of the United States would be greatly eased even if the total U. S. payments deficit were not affected. But it would be rash at this time to pin great hopes on such a development.

Mr. Young presented the following report based on his attendance last week at a meeting in Paris of Working Party 3 of the Economic Policy Committee of the Organization for Economic Cooperation and Development:

This meeting was largely directed to close scrutiny of the U. S. payments deficit and the relation thereto of U. S. monetary and debt management policy. The tone of the meeting was highly critical of U. S. financial policy.

This critical tone no doubt reflected in part the disappointingly large size of the U. S. deficit for 1962 and the inability of the European experts to foresee any sizable reduction in our payments deficit for 1963. It no doubt reflected, too, some disillusionment on the European side as to how soon the U. S. economy would benefit from and respond to the stimulus of a tax cut, with resulting possibilities for less easy U. S. monetary conditions and some rise in U. S. interest rate levels. I earlier reported to you that they regard these developments as essential to restoring U. S. payments equilibrium.

The central theme of the European attack was that the continuing large U. S. payments deficit, whatever its other contributing causes, is being aggravated and prolonged by a net capital outflow that stems in part from excessive domestic liquidity. While this high level of liquidity may have resulted more from heavy financial savings flows than from money creation by the central bank, the Europeans feel that monetary policy is shirking its appropriate role of absorbing excess liquidity.

Debt management, according to the Europeans, must also take some responsibility for continuing payments deficit. It had been financing short a budget deficit in order to support short-term interest rates. Thus, it had failed to bid directly for long-term savings, and thereby had furthered conditions in long-term markets, including interest rate levels, conducive to capital outflow to foreign borrowers.

Since U. S. monetary and debt management policies, according to this theme, were functioning in a way to permit if not encourage, a sizable seepage or spill-over of U. S. savings funds into international markets, European central banks could hardly be expected to help the U. S. finance its payments deficit. Correction of the situation was up to the U. S. authorities. They should no longer delay. In fact, avoidance of delay in action was crucial because of waning confidence in the dollar.

The attack on U. S. policy was supported in varying degree by all of the delegations of countries in payments surplus. The only support for the U. S. position came from two other countries with high unemployment and payments deficit problems--the U. K. and Canada.

The delegations of these two countries gave the U. S. their support on grounds that the U. S. was making progress in meeting its payments deficit problem; that it needed time to adjust its payments position; that domestic economic

factors in the U. S. did not justify restrictive monetary and debt management action at this juncture; and that prospective world demands for goods and services were not so buoyant that any dampening of the U. S. market via monetary restriction could be regarded with equanimity. In addition, the Canadians pointed out that Canadian borrowing in U. S. markets was essential to cover Canada's current account deficit and that Canada's own monetary policy was and had to be geared accordingly.

The head of the U. S. delegation gave an extended explanation of the main factors accounting for the U. S. payments deficit and of the national policies that were being pursued to achieve correction. He laid particular stress on the U. S. directing its policies at fundamental forces of imbalance and eschewing policies that involved direct governmental interference with market processes. To lay the foundation for a better export performance, Government policies had been aimed at maintaining relative price and wage cost stability, more widespread educational and promotional efforts among potential exporters, and more competitive export credit programs.

As to Government expenditures abroad, he underscored the efforts being made to hold down military outlays, to tie aid, and to control foreign expenditures of other governmental agencies.

On capital movements and their sensitivity to higher U. S. interest levels, the U. S. spokesman thought that the domestic credit demands would be more responsive than foreign demands would be, but he recognized the need for a close relationship of U. S. short-term rates with those in other markets, arguing that maintenance of such a relationship was already a phase of U. S. policy and on the whole a successful phase. He further stressed that U. S. credit ease this past year was more the result of a large increase in financial savings by the public than of easy monetary policy and that our money supply increase had been small in comparison with increases experienced by most European countries.

As the U. S. spokesman saw it, the tax program, fundamentally, had the object of increasing domestic incentives to invest, thereby stimulating domestic demands for savings. Until this stimulus took hold, the U. S. probably had to get along with some continuing net outflow of capital, and an accompanying payments deficit. The U. S. authorities hoped and believed that the deficit for 1963

would be significantly smaller than in 1962. Part of this smaller deficit, he suggested, might be financed by U. S. Government borrowing abroad, part by larger holdings of dollars by some countries, and part by gold outflow.

The Chairman's summary at the close of the first day's discussion, but not significantly modified the next day, indicated that there was agreement that U. S. payments equilibrium had to be reached soon, but without steps that might interfere with domestic expansion or otherwise do harm to the U. S. or the world economy. At the same time, domestic U. S. expansion would not by itself bring external payments equilibrium, and consequently monetary policy, which up to now had been primarily domestically oriented, might need soon to give greater attention to the correction of external disequilibrium. The summary stressed the differences of view as to whether monetary policy should be adapted promptly or await enactment of the tax cut.

The Chairman gave his personal view that, while the U. S. might be able to borrow surplus dollars from some European central banks for interim balance of payments purposes, such accommodation on any scale would not be appropriate unless and until U. S. fiscal and monetary policies were oriented in a way that would definitely foster and help to produce a payments equilibrium. He observed in conclusion that when a country's financial policies are regarded as appropriate, its trading partners have an obligation to assist in bridging the presumably short time span necessary for such policies to bear fruit.

No official record is kept of the Working Part 3 discussion, and therefore no minutes will be available as a report of the meeting. Each delegation takes such notes as it pleases, and this resume is therefore no more than a summary of personal and other U. S. notes. It was agreed at the close of the meeting that no report of the discussion about U. S. policy would be communicated by the Chairman to any other OECD body.

The next meeting of Working Party 3 is scheduled for late April. The U. S. deficit problem will again be on the agenda of that meeting, with a Secretariat paper on the U. S. situation to be developed in the interim. The meeting will also have on its agenda, however, a review of barriers to foreign borrowing and capital outflow in such surplus countries as France, Italy, and possibly Germany. This is a subject that the U. S. delegation has long pressed for agenda listing and discussion.

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In reply to a question, Mr. Young said that all of the principal European countries were concerned about inflation and cost increases. They felt that in part these problems reflected their balance of payments surpluses, which they ascribed in turn to the U. S. balance of payments deficit. They considered themselves handicapped, primarily because of external influences, in going forward with the kinds of policies called for by their own domestic situations at the present time. Although various countries had sterilized their gold and dollar reserves to a degree, monetary increases were occurring at annual rates of 10 or 12 per cent or more. They maintained that they did not have the same latitude in this regard as the United States.

The Chairman then called for the usual go-around of comments and views with respect to economic conditions and monetary policy beginning with Mr. Hayes, who presented the following statement:

A number of current statistical indicators were on the down side in January, emphasizing the hesitancy that has been characteristic of the domestic business situation. Such hesitancy is not, of course, unusual in the early months of a new year, and especially bad weather and strikes may have played a part in producing some of these declines. Moreover, a number of other elements continue to indicate a moderate degree of strength, such as consumer spending on automobiles and consumer intentions to buy in the future. New orders for durables took a turn for the better, fourth quarter plant and equipment spending turned out to be a bit higher than expected, and available fourth quarter profits reports look rather good. On balance the outlook is probably still for a continued moderate advance in over-all activity but, partly because of disappointment and uncertainty as to the tax program,

business optimism has probably diminished a little in the past month or two.

Recent bank loan data confirmed the earlier impression that the loan run-offs in January largely offset the unusually substantial loan expansion in December and that the underlying strength of loan demands has not shown any marked change for some months. Such net improvement as has taken place since the beginning of December has centered in security loans and loans to sales finance companies, with business loans showing no real vigor. Data for the first three weeks of February may possibly lend themselves to the interpretation that a somewhat better "tone" of loan demands is currently developing. In general, liquidity continues to be ample.

It may be worth noting in passing that there has been a sizable increase in stock market customer credit since the cut in margin requirements last July, the current level of about \$5.6 billion being 14 per cent above the level at that time. I share the feeling of uneasiness that has been expressed from time to time by the Chairman over the possibility that easy credit availability may have given undue impetus to speculative activities in the last year or so, especially in the real estate area.

While there are only fragmentary data as yet on the February balance of payments, they seem to point to a continuing over-all deficit at roughly the same annual rate as the last couple of years, which is certainly not good enough. Another careful reappraisal of the 1963 outlook by the Government's balance-of-payments technicians yielded a set of forecasts anticipating a deficit ranging from \$2.5 to \$3.9 billion as compared with the \$3.7 billion deficit recorded in 1962 before taking into account certain special transactions. I have found especially disturbing the tendency in the last six months or so toward a somewhat weaker export position, when many had counted on stronger exports as the principal key to payments equilibrium. This situation suggests the vital need for strict control of costs and lends weight to Per Jacobsson's recent proposal that this country should try to achieve stability in money wage rates rather than progressive wage increases geared to average national productivity gains, in order to bring down rather than merely to stabilize its cost structure.

The outflow of gold was resumed last week and the prospect is for substantial gold sales during the coming months. No other results can be expected with the over-all payments deficit at its present level. Although there can

be no precise measure of what constitutes the danger point for our gold stock in terms of the psychology of persons and institutions, both here and abroad, capable of moving large funds out of this country, we are clearly getting closer to the danger point as the gold stock diminishes while the balance of payments deficit continues unabated.

I remain convinced that diminished credit availability and somewhat higher interest rates, particularly for short-term maturities, can make an important contribution to a better balance of payments position, partly because of the psychological effects that such tendencies might have on thinking, both here and abroad, with respect to the outlook for the dollar. In passing I might say that I do not share Per Jacobsson's faith in a continuing downward trend of interest rates in Europe, which he counts upon to make easier the maintenance of low rates in this country. There is no reason to believe that some of the European countries will refrain from restrictive measures either to cope with the danger of serious inflationary price and wage trends or to prevent the development of appreciable drains on their monetary reserves. Already in France there has been a start on such restrictive actions.

Admittedly a move toward lesser ease would involve some risks with respect to the domestic economy, but I believe they are minor risks in comparison with the growing danger to the dollar's international standing. It would be highly desirable to have any decisive move toward less ease on the part of the System receive the support of the Administration. Also, having in mind that monetary policy by itself cannot hope to cure a balance of payments deficit of the magnitude in question, I would hope that such a policy move would be accompanied by decisive actions in other areas on the part of the Administration to reduce the balance of payments deficit. But unless the System is prepared to play its part, it can hardly expect to see a concerted and effective attack on what I believe to be our most critical financial or economic problem.

As we are in the midst of the Treasury's advance refunding, in which market participants have extended maturities and dealers have acquired large positions that need to be worked down, we must obviously avoid any policy changes for the time being. However, shortly before the next meeting of the Committee there might be an opportunity for a start on open market operations designed to reduce somewhat the current degree of monetary ease. There might also be an opportunity late in the month for an increase in

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the discount rate, if the System were willing to give a clear signal of its concern for our international position. Alternatively, the latter half of April should provide a "free period" when action of this kind might be considered-- obviously with due consideration to any changes in underlying conditions that may have occurred in the interim.

With respect to the directive, it would seem to be appropriate to change the wording somewhat, even in the absence of the slight change of policy I am proposing, if for no other reasons than to demonstrate that the directive's wording does not have the same "frozen" quality as the former (b) clause.

In reply to inquiry by the Chairman as to whether he had specific suggestions for modification of the current economic policy directive, Mr. Hayes said that he would recommend inclusion in the first paragraph of a sentence stating that the current policy of the Committee recognized that achievement of a balance in the international accounts of the United States was required to assure a sound continuing growth of the domestic economy. Such a sentence would give recognition in the directive to what was in his opinion a most important consideration, namely, that lack of balance in this country's international accounts was a great shadow over the domestic economy and that the achievement of a balance in such accounts was required to assure continuing domestic economic growth. Mr. Hayes also recommended changing the second paragraph of the directive to specify that open market operations during the next three weeks would, as soon as practicable consistent with Treasury financing operations, be conducted with a view to maintaining a slightly greater degree of firmness in the money market than in recent weeks.

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Mr. Shuford observed that domestic business activity apparently was continuing at about the same level that had prevailed for the past several months. The broad measures of economic performance did not seem to have broken out of the narrow range in which they had moved since last summer. A similar situation existed in the Eighth District, where there had been no significant changes from the levels of last fall and early winter. Employment showed no change since November, the level being slightly lower than last summer but a little higher than a year ago. Industrial use of electric power and department store sales had changed little in the past nine months, although each was somewhat higher than a year ago. In the financial area, preliminary figures indicated that total deposits were about unchanged from January to February. Business loans appeared to have declined somewhat.

Mr. Shuford commented that monetary developments in the nation, as well as fiscal developments, had been expansionary during the latter part of 1962. The rates of increase in bank reserves, bank credit, and the money supply were greater than appeared to be desirable for any extended period of time. Since December, however, monetary developments had been less stimulative. Reserves in support of private demand deposits had declined, and the money supply had risen at a reduced rate.

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Mr. Shuford went on to say that his uneasiness with regard to the balance of payments situation had increased during the period since he began attending meetings of the Open Market Committee regularly several months ago. There appeared to have been no significant improvement in that situation, and it might be necessary at some juncture to take steps of a more positive nature than any taken in recent months. It seemed to him, however, that corrective steps in areas other than monetary policy were necessary if the fundamental problem was going to be solved. Monetary policy must play a part, and at the appropriate time it might be necessary, as he had indicated, to take more positive steps. He hoped, however, that if actions were not instituted in other areas first, at least they would be taken in coordination with monetary policy actions.

As to monetary policy for the short-run future, Mr. Shuford said he would favor no change. He would like to see a continuation of about the same degree of money market firmness that had prevailed during the past several weeks. He would favor no change in the discount rate at this time. (In this connection Mr. Shuford mentioned that there had been a brief reference to the possibility of a discount rate increase toward the end of the most recent meeting of the St. Louis directors. He did not know what conclusions the directors might reach if the matter was explored more extensively.)

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Mr. Bryan said that the trend of Sixth District employment figures had changed very little. On the other hand, personal income had increased somewhat. Bank loans and investments were rising; the financial series were strong. He did not find evidence in the District or in the nation that the economy had moved very much or that it was clearly poised for a decisive move in either direction.

As he saw it, Mr. Bryan said, no change in policy was called for at this time. The reserve picture struck him as quite appropriate. The supply of reserves was above the guideline used by the Board's staff and slightly above the guideline that he (Mr. Bryan) had been using. He would not change the discount rate at this time.

As to the balance of payments, Mr. Bryan said that he was indeed concerned. However, he would like to play on a team, so to speak, and he would like to see more things done outside the area of monetary policy. If other corrections were made, he would favor the use of monetary policy in a complementary way. At present it appeared to him that about the only thing monetary policy could seek to accomplish would be to diminish capital outflows, which would require substantial interest rate increases in order to be effective. If foreign aid and perhaps military expenditures could be reduced further, and if American citizens were discouraged from excessive travel abroad, then he would want to take action in the area of monetary policy. Under present circumstances, however, he thought it would be perilous for

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the System to undertake the deflating of the domestic economy that in his opinion would be necessary to reduce capital outflows sufficiently to provide a solution to the balance of payments problem.

Mr. Bopp said that in advance of this meeting he had prepared a statement for presentation. However, he had been influenced by the discussion that had taken place this morning. Accordingly, instead of the somewhat more stimulative monetary policy that he had intended to advocate, he would now favor no change in policy for the next three weeks. At the same time, the paper that he had prepared suggested the general tenor of his thinking, and he would like to read it. Mr. Bopp then presented the following statement:

As one looks at the economy in early March, it is hard to distinguish the real situation from fluctuating moods and sentiment. When it comes to business conditions in a Federal Reserve District, we have the further complication of lagging information. Business in the Third District probably worsened in January, but there are some inconsistencies in the available bag of indicators. Although unemployment is up again and total employment has not increased for some time, the demand for labor (help wanted ads and average work week) may have strengthened a little in December and January. Since January, unemployment claims have decreased seasonally and steel production has rebounded, indicating that February may have seen some slight improvement in Third District economic activity.

This tentative possibility is supported by banking developments. Loans turned up in the last two weeks, halting the typical seasonal decline. This upturn, brief as it has been so far, seems quicker and more sharply defined than in comparable periods in recent years. Last year there was no definite sign of loan expansion, following the seasonal reductions after the turn of the year, until at least March. In 1961 there was no definite loan expansion until April. Business loans, loans to sales finance companies, real estate loans, and the "all other" category have climbed over the last two weeks.

In short, changes in the level of activity in the Third District have been modest and mixed, as has been true in the country as a whole. Unfortunately, the general level at which these changes are taking place remains at the inadequate plateau reached last summer. I agree that it would be appropriate to stimulate aggregate demand by means of tax reduction. What we have had, however, is considerable talk of tax reduction accompanied by actual increases in Governmental revenues via social security and higher postal rates, temporarily offset in January by VA insurance dividends. To me this means that until we secure actual relief from fiscal policy, monetary policy will continue to have to bear a disproportionate share of our total program to stimulate demand.

Our current directive is permissive of moderate growth in bank credit and in reserves. Meanwhile, we have more than adequate raw materials, plant, equipment, and manpower to support expansion in real terms. Under these circumstances, it seems to me we should stimulate the demand for credit rather than accommodate the supply to autonomous increases in demand.

There is a risk in such a program, especially internationally. Some feel also that additional credit would go to wrong uses. For my own part, I am willing to rely on the market to distribute the credit, in the belief that lenders are sophisticated and desire repayment of principal as well as interest.

In conclusion, I am unhappy with our over-all economic program. I wish the mix were different. I would support a different monetary policy as part of an over-all program directed toward both our domestic and our international problems. As of today, however, I do not see prompt development of such an over-all program; and therefore, reluctantly, come to the conclusion that a somewhat more stimulative credit policy is appropriate.

In conclusion, Mr. Bopp repeated that in light of the discussion thus far at this meeting he would recommend no change in policy at the present time rather than the shift in policy recommended in his prepared statement.

Mr. Fulton reported that business activity in the Fourth District was perceptively on the upgrade in February despite continued

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harsh weather. New auto sales ran above the January level; used car sales also were satisfactory, with steady prices and reasonable inventories. Department store sales sagged further on a seasonally adjusted basis, with a five-week moving average standing at the lowest level since last mid-July. It was felt, however, that continued snow and cold had been a major contributor to this situation.

Steel ingot production had expanded considerably in the District, but not quite as much as nationally. New orders had increased, indicating inventory building on the part of users. The mills themselves were producing some ingots for their own inventory, to be finished later on order. Discussions with businessmen revealed hedge buying against a strike, which was likely to have an adverse effect on production in the last half of the year.

Construction activity had moved up sharply in the District; several large projects had increased the total for both commercial and residential buildings. Despite continued cold weather, the rate of insured unemployment in the District declined in all but one of the major labor market areas during the first three weeks of February. On a seasonally adjusted basis, the total was 5 per cent lower during the week ended February 23 than it had been in any previous week this year. The greatest improvement occurred in the steel-producing areas.

The decline in loans thus far in 1963 had been slightly larger than in previous years, reflecting a sharp drop in loans on securities

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and a smaller than usual increase in consumer loans. Business loans had declined at about the same rate as in the past two years. The decline in total deposits was less than in previous years due to different patterns of public and time deposits.

As for monetary policy, Mr. Fulton felt that a continuation of the level of free reserves and short-term interest rates that had existed in the past three weeks would be appropriate for the coming period. He would not propose a change in the discount rate. In the directive, he would remove the phrase "and in view of the forthcoming Treasury financing" in the first sentence of the second paragraph. Otherwise, the directive seemed to him to be appropriate.

Mr. Mitchell said it seemed to him that the staff description of the domestic economic situation was accurate. There had been substantial monetary expansion in the last quarter of 1962, but it had not yet resulted in enough economic action to provide assurance that the economy was definitely on the upturn. In view of this uncertainty, he did not believe a change in monetary policy at the present time would be justified by domestic considerations.

On the balance of payments side, Mr. Mitchell said, he was more optimistic than in a long time. That was not due to anything this country had done; instead, it reflected the difficulties of this country's principal competitors. He felt that the possibilities mentioned by Mr. Furth had a chance of being realized this year. The

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trading position of many countries was deteriorating, and Common Market developments seemed to have had at least a psychological impact favorable to the dollar. Further, Americans might be having second thoughts about investing abroad due to political and economic developments.

After comparing the restrictions in European capital markets with the relatively free capital markets in this country, Mr. Mitchell expressed the view that the maintenance of the short-term interest rate was generating the kind of abnormalities in the U. S. economy that had been generated by pegging the price of Government bonds prior to 1951. The support of the short-term rate perhaps had not reached a critical stage, but he felt it was an abnormality that had a worsening influence on current problems. With liquidity at a high level, it was desirable and possible to achieve some funding if the gap between short- and long-term rates could be widened.

Advice was being received from Europe that long-term rates should be increased. Obviously, however, that would come as a shock to the confidence of the American people. If investors in this country came to believe that the Federal Reserve was fixing interest rates all along the maturity line, there would be serious misunderstanding of its function and operations. The basic balance of payments problem was certainly serious, but he would like to see action taken on other fronts. He did not believe that too much was going to be accomplished just by protecting the short-term rate. Recently he had made certain suggestions

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about tax considerations, and since that time many people had been talking to him in terms that tax considerations were important in many fields. They appeared to have a distinct bearing on decisions as to where money would be placed in the world's markets.

If he thought the balance of payments problem really could be corrected by the use of monetary policy, Mr. Mitchell said, he would favor doing as much as possible, but he did not believe this would provide a solution. On the other hand, monetary policy could be of some help in relation to the domestic situation. At the present moment he felt that monetary policy was doing enough in the latter regard, but it might be called upon to do more before long, partly due to the uncertainty about passage of the Administration's tax proposals and the question whether, in any event, such action would provide too much or too little of a stimulative effect. In substance, monetary policy seemed to be about the only tool available to encourage the domestic economy to expand. As he had said, however, it was his conclusion that at this particular time monetary policy need not be changed. He would be willing to modify the policy directive in accordance with any of the suggestions that had been made except those of Mr. Hayes.

Mr. King noted that he had been more or less out of touch with economic developments during the past several weeks. Therefore, he had no particular recommendation as to monetary policy at the present time.

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With respect to the policy directive, it appeared that one or two of the technical changes mentioned at this meeting might be appropriate.

Mr. Shepardson expressed the view that the economic situation had been covered well in the staff reports at this meeting. There was uncertainty as to future economic developments. There was also uncertainty as to what might be done by way of implementing some of the suggested approaches to the balance of payments problem. Altogether, the outlook seemed rather unclear at this time. Accordingly, he felt that it would be appropriate to continue the present monetary policy for the next three weeks.

Mr. Robertson stated that his views were very much in accord with those expressed by Messrs. Bopp and Mitchell. In exposition of his thinking, he presented the following statement:

I have been somewhat heartened by the developments since our last meeting. For one thing, the decline in bill rates that has taken place was allowed to proceed without strong counteraction by the Trading Desk to push it back up to its mid-February high. It is no secret that I was concerned lest we fall into a "bill rate only" directive to the Manager of the Account that would require him to oppose bill rate declines even at the expense of restricting reserve availability and tightening general money market conditions much more than was called for by the larger aims of monetary policy. I was glad to see the Manager refrain from any appreciable restrictive action in the face of the bill rate decline of the last three weeks, allowing the technical and expectational factors that were peculiar to the bill market to ease conditions slightly there, without altering the even-keel position in other sectors of the money and credit markets.

I also take some encouragement from the apparent pause, if not reversal, in the contraction in reserve

utilization by the banking system that had seemed to be developing around the time of our last meeting. I continue to think that our domestic business situation is such as to benefit from maintenance of a general atmosphere of credit availability, with bank loan funds abundant and with growth proceeding in the money supply as well as in time and savings deposits. The current business climate, fraught with uncertainties as to tax cut prospects, strike possibilities, and the strength of final demands in some key markets, is not well braced to stand any additional uncertainty regarding possibly tighter money conditions. If, in all these circumstances, businesses appear willing to proceed with a high level of investment (as may be learned in a few days from reports of survey results), then the proper course for policy would seem to be to accommodate and sustain such demands, rather than to take any action that might restrain them.

Our international financial flows are giving us less reason than at other times to curtail money and credit availability. Those kinds of flows that might be deemed most susceptible to moderate changes of monetary policy are less troublesome currently, and the relevant bill rate differentials are, if anything, mildly encouraging to a flow in our direction. This is a good time, I think, to reiterate two points concerning our capital flows. First, rate relationships between U. S., Canadian, and U. K. bills are such that any significant unilateral rise in the U. S. bill rate might even lead to some inflow of funds from Britain and Canada. In the current economic and political circumstances of both countries, sizable reserve losses to the U. S. are not, I submit, desirable--and certainly not something that we should be taking deliberate action to create. Second, capital outflows, for all their reserve impact, are not an unmixed evil. Unlike trade deficits, capital outflows have inherent in them some return flow prospects. Interest and dividend earnings accrue, debts have to be repaid, and equity investments abroad are sold from time to time. As time passes, the return flow of funds to the U. S. is bound to rise, and it is very hard to believe that such a rise will not more than keep pace with gross new capital outflows, particularly with some recipient countries uneasy about the size of foreign capital investment. Thus, in a real sense of the word, net capital outflows can be eventually self-dampening.

I do not assert that this characteristic of capital flows permits us not to worry about them at all. My point is that we do not have to set monetary policy as if it were the only brake upon a potentially limitless and use-less outflow.

With all these considerations in mind, it seems to me that the best course for monetary policy over the next three weeks is to hold more or less a steady course. I suggest that the resolution of doubts be on the side of ease; but no greater policy change would seem practical considering the current Treasury financing.

I am concerned, however, that our directive to the Manager be such as to suggest the Committee's operational intent fairly and as concretely as feasible. To that end, I should like to suggest the following somewhat more explicit language as a substitute for the second paragraph in the present directive:

"To implement this policy, operations for the System Open Market Account during the next three weeks shall be conducted with a view to maintaining marginal reserve availability at about the average level thus far this year, fluctuating as necessary to moderate marked swings in money market conditions and to partly offset any tendency for aggregate reserve expansion to deviate substantially from the average rate for 1962 as a whole."

To give you a concrete idea of the reserve statistics which this kind of directive would be asking the Desk to keep in mind, let me report that thus far this year free reserves have averaged about \$330 million and borrowings around \$135 million, and that total reserve expansion for the year 1962 as a whole averaged a shade over 3 per cent, if you include the reserves freed by the reserve requirement reduction last fall. I would not want to include these specific figures in any directive, because I would not want either the Manager or the public to be led into thinking that the Committee wished to achieve any precise statistical objectives, or that it had any illusions that the Manager could in fact hit such statistical targets even if they were desired. Rather, I think the purpose of our directive should be to suggest, in clearly objective terms, the kind of money market and reserve climate that the Desk should be seeking to achieve and the general way in which the Desk should modify its operations if results do not turn out as desired.

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Mr. Mills said that as he surveyed the areas for policy determination by the Open Market Committee, it appeared that at present they had been narrowed and were conditioned by Treasury operations. The success of the Treasury's advance refunding might have a darker side in that, by removing a certain volume of relatively short maturities into the longer term areas, there was the possibility of downward pressure being exerted on the short-term interest rate. If such a development should occur, it would leave the Federal Reserve in the unenviable position of choosing whether to support the short-term interest rate in an effort to keep it at some particular level or whether to allow the rate to fall to a level determined by market factors. The second alternative would be his personal choice, because he felt that too great a preoccupation with maintaining the interest rate structure would be likely to put pressure on the money supply at a time when it should be maintained or encouraged to increase. Fortunately, the unwinding of dealer positions in the refunding operation would produce a cushion that might absorb additional demands for credit without undue tightness.

Mr. Mills reiterated the concern he had expressed on previous occasions that a pegging of the short-term interest rate gave a false picture of the state of the Government securities market and other securities markets. If it were abandoned, he felt that the sensitiveness of a free market would produce a realistic short-term rate of interest, one that would be found not to be out of line with balance of payments considerations.

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As to the balance of payments, Mr. Mills said he was among those who felt that monetary policy was not a panacea for correction of the problem. He thought that primary responsibility must rest with the Treasury Department and that strong measures might be called for in the near future, in which event monetary policy would be principally a coordinate to the broader policies that would have to be adopted.

Referring to the remarks of Mr. Bopp, Mr. Mills expressed concern that the availability of credit be adequate to sustain the money supply. The uses of that credit could not, of course, be controlled by the Federal Reserve System, acting within its present field of responsibility; the System could not determine whether the credit would seep into undesirable speculative areas, real estate or otherwise. This was a problem that might have to be faced through reconsideration, at some rather remote time, of selective credit controls.

For the moment, Mr. Mills said, he would favor no change in monetary policy. Neither would he favor a change in the discount rate. As to the policy directive, he found himself disillusioned. The changes in wording seemed to have become almost a matter of gamesmanship. Various changes were made, but when the movements in reserve statistics were measured against the words of the directive, he found it difficult to see a correlation.

Mr. Wayne reported that recent statistics and survey returns suggested some general improvement in Fifth District business conditions.

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Seasonally adjusted bank debits, nonagricultural employment, and manufacturing man-hours rose in January following December declines. While recognizing the limited significance of regional developments during a single month, it was interesting to note that factory man-hours rose sharply counter to the national trend as broadly based increases reached substantial proportions in chemicals and several lines of durable goods. Recent developments reflected in the Reserve Bank's survey included a small rise in optimism among businessmen generally and some improvement in the demand for bituminous coal. In the textile industry, however, current operations continued to be hampered and the outlook remained clouded by the enigma of what Government action, if any, would be taken to eliminate the difference between domestic and export cotton prices. Textile orders had been light for several months and inventories, although high at the mills, were said to be low in distributive channels. A solution to the raw cotton price problem would eliminate most of the current uncertainty, but prospects of reaching such a solution had steadily worsened.

The national economy, Mr. Wayne observed, seemed to be continuing its general horizontal movement. Since the first of the year there had been moderate gains in several major sectors of the economy but, as Mr. Noyes had already noted, in most sectors activity had been fluctuating around levels first reached some six or eight months ago. At the same time there had been a few substantial declines and an

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accumulation of small declines, which might raise a question as to the strength of the present stability. Also, the hope for a tax reduction, which had been a sustaining element for several months, seemed to be fading as prolonged discussion made it more and more apparent that decisive action would be long delayed and would provide little stimulus this year. All of these considerations certainly did not indicate that a precipitate decline was just around the corner, nor did they suggest any breakout on the up side. To him the prospects were for a continuation of the game of plus and minus, but the Committee should be alert to any increase in the number of minus signs.

In the policy area, Mr. Wayne noted that there was still little room for maneuver. With the Federal funds rate sticking closely and firmly to the ceiling for almost a month and the bill rate not far below it, except for a short period dominated by special developments, there could be very little tightening without raising the question of a hike in the discount rate. To raise the discount rate or even to create conditions that would generate widespread speculation about such a raise would, he believed, be a serious mistake from all points of view. In the other direction there might be a little more elbow room, but to utilize it would quite likely cause the System to forfeit the slight improvement the dollar had accomplished in relation to the Canadian dollar and the pound sterling in recent weeks. Also, any easing that could safely be tried would not be sufficient to have any

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appreciable effect on the domestic economy. Since basic conditions had not changed significantly since the previous Committee meeting, he favored a continuation of present policy and renewal of the current directive, except to eliminate the reference to "forthcoming Treasury financing." He would not change the discount rate, as his previous remarks indicated.

(Mr. King withdrew from the meeting at this point.)

Mr. Clay reported that the recent trend of nonfarm economic activity in the Tenth District presented a close parallel to the national picture. This similarity included the fact that substantial variation existed among the various metropolitan areas. Employment, after accounting for seasonal movements, was being sustained at record levels. As had been the case nationally, Tenth District employment in Government and in service and distribution industries was advancing, while manufacturing and most other goods-related activities were experiencing reduced employment levels. The decline in manufacturing employment since mid-1962, however, had been only about half the national rate. Construction employment also was holding up better in the Tenth District than across the country. This was related, in turn, to the somewhat stronger rate of contract-letting last year in the Tenth District, where gains relative to the nation were notable in awards for nonresidential construction and for public works and utilities.

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The volume of farm marketings in the Tenth District seemed likely to remain high during 1963 because of an anticipated record level of marketings of livestock. Cattle numbers had increased 25 per cent in the District since 1957, compared with a 14 per cent increase for the nation as a whole. The outlook for crop production was less favorable than a year ago because of deficient supplies of surface moisture in a major part of the area. With normal spring rains, however, crops, along with pastures, could improve rapidly.

It now appeared that prices of most major farm commodities produced in the Tenth District would be lower than in 1962. Unless crop production (a major proportion of which was subject to price supports) should turn out to be unusually good, cash receipts from farm marketings this year were expected to be somewhat less than in 1962. Government payments to farmers, however, were likely to be higher because of the certificate payments to be made to producers cooperating with the wheat and feed grain programs. Barring an extensive drought, gross farm income in the Tenth District might approach the 1962 record. It would take unusually favorable conditions, however, for gross farm income to surpass last year's record.

So far as monetary policy was concerned, Mr. Clay noted that the Committee continued to face the same kind of dual domestic and international economic problems with which it had been struggling for many months. Perspective for the future was not very clear on either

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of these problems. It was clear, however, that the domestic economy remained sluggish in its performance and that this country's international balance of payments remained seriously adverse. As perspective became clearer, the resolution between alternatives might become more apparent. For the present, it would appear to him appropriate to pursue essentially the same basic policy that had been the Committee's goal in recent weeks. Pursuit of this policy until the next meeting of the Committee would, he suggested, have as targets 2.85 to 2.95 per cent for the Treasury bill rate and 3 per cent or slightly less for the Federal funds rate. It would be the intent to supply member bank reserves in sufficient amount to permit moderate bank credit expansion on a seasonally adjusted basis. No change in the Reserve Bank discount rate would be contemplated. While the general posture of policy would be in line with the present directive, he felt that the directive should be rewritten so as to avoid a cumulative restriction of bank credit in view of the current reference to recent months, presumably referring primarily to late 1962.

Mr. Scanlon reported that there had been little change in the level of employment and retail trade in the Seventh District thus far in 1963. Steel output was continuing to increase as steel users began to build inventories. About 55 per cent of the purchasing agents of Chicago who buy steel as a "major production item" intended to increase steel holdings as a strike hedge, according to a recent survey. The

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improved level of steel orders was reported by people in the industry to be broadly based, with railroad car builders and structural steel fabricators among the industries increasing their orders.

Auto output had begun to decline gradually despite a continuing high level of sales. Inventories of new cars probably reached about 1,050,000 at the end of February. This was a record level for the period and was surpassed only by a few months in the middle of 1960. Manufacturers probably would not permit any further increase of inventories, and production schedules would be set on the basis of daily sales.

A number of capital goods producers had reported good order trends in December and January. This was true of railroad equipment, farm and construction machinery, trucks, and some types of industrial equipment. There had been reports also of a sharp rise since November in orders for gears, bearings, and hydraulic drives--items that are used mainly in the manufacture of capital goods. New orders of these firms had tended to "lead" capital goods output in the past.

Developments at Seventh District weekly reporting banks indicated there had been some slowing of credit demand by business and consumers compared with the latter months of 1962. Most of the growth in total loans over the past month had been in dealer loans secured by U. S. Governments, and reflected unusually large portfolios of such loans at several District banks. On the whole, reserve positions of the money

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market banks had been quite comfortable, and the major portion of Federal funds purchases had been by one bank. Borrowing at the discount window had been nominal.

With the usual increase in business needs for funds in March, and possible further Treasury borrowing, Mr. Scanlon felt that it should be possible to maintain short-term rates while obtaining some further reserve expansion. Therefore, the existing directive appeared appropriate to him, except that he would change the reference to timing of the Treasury financing. He would not favor a change in the discount rate at this time unless it were to be part of a package that would include corrective balance of payments action in areas outside monetary policy and would be a clear signal to the world of this country's intent to defend the value of the dollar.

Mr. Deming reported that Ninth District economic activity had held up well during the first two months of 1963 despite unusually cold weather. January personal income ran at a rate 7 per cent ahead of a year earlier, and on a seasonally adjusted basis was almost 1 per cent ahead of December, both gains better than those registered for the country as a whole. Nonagricultural employment in Minnesota in February was 0.6 per cent larger than in January, seasonally adjusted, and for the first two months of this year averaged 2.3 per cent higher than in 1962. Department store sales were running 3 per cent higher than last year. Manufacturing activity, particularly in durables, seemed

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to be fairly strong; construction, considering the weather, was surprisingly strong.

The Reserve Bank's opinion survey taken late in February showed little change in expectations from the survey taken five weeks earlier; 48 per cent foresaw improvement as probable or certain over the next several weeks, 37 per cent foresaw continued stability, and 15 per cent foresaw some decline. The group foreseeing decline in the near future was of about the same magnitude as in all surveys taken since early last fall. The shift in outlook since year end reflected a rise in numbers seeing continued stability and a fall in those foreseeing expansion.

Recent data on District banking indicated that the loan and deposit weakness in January at city banks did not continue into February. Loan increases in the first three weeks of February pointed to a new record for the month at those banks; the decline in investments was smaller than usual (although larger than in 1961 and 1962) and total deposits apparently would be up for the month, whereas they usually decline. Country bank data for the first half of February indicated normal seasonal movements.

As to policy for the short run, Mr. Deming said he would be inclined to "stay about where we are" during the next three weeks. Consequently, he would not wish to change the policy directive to any significant extent. He was not even sure that it would be necessary to

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delete the reference to the "forthcoming Treasury financing," although it was true that the language now in the directive was intended to refer to Treasury financing different in scope from the prospective financing during the next three weeks. He would not recommend changing the discount rate at this time.

Looking somewhat further ahead, Mr. Deming indicated that he would like to associate himself almost completely with the comments of Messrs. Mitchell and Robertson on the balance of payments. He was particularly impressed by Mr. Robertson's comments about the U. S.-U. K.-Canadian triangle. Money chasing itself within this triangle would appear to have no real effect, except statistically, on the U. S. balance of payments. Canadian borrowing in U. S. markets in February had evidently accounted for a substantial part of the U. S. payments deficit in that month. He was glad that that had been pointed out at the Working Party 3 meeting.

Mr. Deming noted that it was possible to advance a hypothesis that there was "overly excess liquidity" in the American financial system, leading to some spillover into foreign loans and investments and hence into capital outflows. Should this be the case, it might be possible to follow a monetary policy aimed at mopping up some of the overly excess liquidity without any appreciable affect upon the availability of funds for the domestic economy or upon domestic interest rates. Such a policy, which he would not advocate for the time being,

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would be implemented by aiming at somewhat lower free reserve levels-- and perhaps would result in somewhat higher member bank borrowing levels--without attempting deliberately to aim at a higher interest rate structure. If such a program led to somewhat higher rates, they would not be resisted strongly, but they would not be sought.

Mr. Swan reported that in January there was a drop in the overall rate of civilian unemployment in the Pacific Coast States from 5.7 per cent to 5.4 per cent, which was the lowest rate since April 1960. Increases in employment reflected substantial gains in construction, services, and manufacturing. The gains in manufacturing employment occurred despite the fact that ordnance and aircraft, two defense-related industries, showed small declines. However, in the electronics group, which is also considered defense-related, there was a continuance of the rapid growth of employment that had been experienced for some time, with the January figure more than 12 per cent above the figure for a year earlier.

Available data for February were, of course, extremely fragmentary. However, department store sales, which in January returned to the previous high of November, apparently were well maintained in February, while Western steel production increased in the first three weeks of the month. There still seemed to be plenty of funds seeking investment in the real estate area. Share accounts and real estate loans at savings and loan associations increased more rapidly in the

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District than in the nation from December to January. Both were about 24 per cent above January 1962, which again represented a somewhat larger increase than for the country as a whole.

District weekly reporting banks showed a good loan increase in the first three weeks of February. In this period, they switched from the status of net buyers of Federal funds to net sellers on a rather substantial basis. However, this did not seem to reflect any change in their basic reserve position; instead, it reflected a shift of some larger banks from Treasury bills to the Federal funds market in view of the higher rates available. In fact, District weekly reporting member banks accounted for virtually the entire decline in holdings of Treasury bills and of all Government securities at all weekly reporting banks in the country in these three weeks.

Turning to national economic developments, Mr. Swan noted that there was no indication of any significant change. Evidence was lacking of a more rapid rate of advance, and no one could anticipate what was going to happen in the area of tax reduction.

In his opinion, a modest tightening of monetary policy would not in itself have any significant effect on the balance of payments problem. Also, the Treasury advance refunding would be in process for a few more days, and there was in prospect an offering of short-term securities around the middle of March. In view of these factors, he would not recommend any change in policy at this time. Instead, he would argue

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for continuation of present policy for the forthcoming three-week period. He would not recommend changing the discount rate.

As to the policy directive, Mr. Swan said his first reaction had been that no change was needed. However, he would support the suggestion that had been made for removal of the reference to the "substantial increases" in bank credit, money supply, and the reserve base in recent months. Two months had passed in 1963, and the substantial increases occurred in the latter part of 1962. He also felt that the reference to forthcoming Treasury financing ought to be changed. The financing operations in prospect were not of the same magnitude as those that had occasioned the inclusion of this language in the existing directive. However, some reference to Treasury financing might be desirable.

Mr. Swan then referred to the remarks that had been made about the possibility of substantial downward pressure on short-term rates as an outgrowth of the advance refunding, due to the reduced volume of short-term securities. There was the possibility, he suggested, of having two conflicting goals, one in terms of maintaining about the same degree of firmness in the money market and the other in terms of offsetting downward pressure on the bill rate. Conceivably, the downward pressure could be so great that the only way to offset it would be by increasing the degree of firmness in the money market. He would not like to see a precipitate drop in the bill rate, but neither would he like to see a substantial firming in the money market solely out of

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consideration of the bill rate. Perhaps, therefore, there would be some advantage if the directive called for "cushioning" rather than "offsetting" downward pressure on short-term rates.

Mr. Irons reported that there had been no noteworthy developments in the Eleventh District. Economic activity continued at about the same level that had prevailed for some time. He was somewhat concerned about scattered conversational references to a possible deterioration in the quality of bank credit, growing out of the desire of banks to increase earnings to meet higher interest rate payments. Also, the booming volume of construction activity, particularly of office buildings and high-rise apartments in the major cities of the District, might warrant some concern. In most respects, however, District trends did not seem greatly different from the national trends. Among more knowledgeable businessmen he saw no particular lack of confidence, but certainly confusion and uncertainty had increased with respect to both domestic and foreign affairs. If this continued, it might lead to some loss of confidence. People seemed more concerned about the budget deficit, the balance of payments situation, and the outflow of gold than they did about a tax cut.

For the forthcoming three-week period, Mr. Irons recommended maintenance of the status quo in terms of policy. He would seek to avoid deviating from the degree of market firmness that had existed. As he saw it, the System had been trying to get at the best of both

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worlds by following a moderate policy course, on the one hand trying to provide reserves for domestic expansion--without going to excess-- and on the other hand trying to be firm enough to minimize capital outflows. He did not know whether the System could do much more until it was found necessary to make some drastic move by shifting the emphasis in one direction or the other depending upon whatever conditions might be present at the time of such decision. He doubted that much was going to be accomplished by minor shadings, such as changes of a few basis points in the short-term rate. Therefore, he would continue the status quo for the time being.

As to the policy directive, Mr. Irons indicated that he tended to agree with the comments of Mr. Mills. He had recently reviewed and compared all of the policy directives issued by the Committee since June 1962, and it appeared to him that the Committee probably could operate satisfactorily today under the directive issued on July 10, 1962. He sensed a growing tendency to feel that the directive should be changed at every meeting, even if only for reason of semantics. When the directives were published, the large number of changes--aside from necessary technical changes--might be confusing. His inclination, therefore, would be to continue the existing directive.

In conclusion, Mr. Irons said that he would not recommend changing the discount rate at this time.

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Mr. Ellis commented that January statistics on unemployment, length of work week, and consumer spending seemed to suggest some slight improvement in New England economic conditions. Basically, however, the situation was unchanged.

Mr. Ellis then referred to three items of information that had been of some interest to him. The first had to do with a retraining program in the Boston area to develop clerk-typists. Some 3,500 persons from the list of job seekers were contacted, but only 243 responded. After further screening only 11 were found to be interested and eligible for retraining. The second piece of information related to the bankruptcy of the American Guarantee Company, which had caused a number of banks to re-examine their lending policies with regard to leasing companies. The firm in question had operated on a national basis, leasing machinery and equipment. It now turned out that the company was extending credit to marginal risks that apparently could not get credit elsewhere, and delinquencies had been covered by the rewriting of leases. As a third piece of information, Mr. Ellis reported that the Boston Reserve Bank was in process of tabulating the results of its regional survey of manufacturers' capital expenditure plans. Preliminary results indicated that outlays in 1963 might be somewhat lower than in 1962, although outlays of nonelectrical machine industries were expected to rise substantially. The survey also suggested that there would be greater reliance on external sources of funds than in 1962.

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Mr. Ellis said it seemed to him that business conditions and business sentiment were about as good as could have been expected during the February-March period when the general outlook was traditionally obscure. The winter, he noted, had been severe in many areas. Conditions continued to be strong enough to support an expansion of the money supply in the face of the monetary policy adopted by the Open Market Committee in December 1962. As he understood the phrase "overly excess liquidity" used by Mr. Deming, this was the same factor that had motivated him (Mr. Ellis) to support the shift in policy in December. He would be prepared to push that policy further if the economic trend became more clear and the economy demonstrated strength in the spring.

As to the balance of payments, Mr. Ellis said that at the moment he was much in sympathy with the comment of Mr. Bryan that he would like to play on a team. Monetary policy had an important role to play if a strongly formulated and executed general policy for dealing with the balance of payments problem was developed. In fact, Mr. Ellis said, he would not be above seeing the Federal Reserve take some initiative in promoting that idea. However, he shared the concern of those who would be apprehensive about vigorous action being taken in the form of monetary policy alone.

For the moment, Mr. Ellis continued, he would support a position of no change in policy. As to the policy directive, he would favor

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eliminating the reference to the "substantial" increase in bank credit, money supply, and the reserve base in recent months. He would also eliminate or modify the reference to "forthcoming Treasury financing."

Mr. Ellis said that he would not favor a change in the discount rate at this time.

Mr. Balderston commented that spring prospects seemed to him to have improved, even if only because of prospective inventory hedging in anticipation of a possible steel strike. He supposed that a price would be paid somewhat later, perhaps in the second half of the year, and that there would continue to be worries emanating from wage negotiations.

Mr. Balderston went on to say that he had been impressed by the comments at this meeting with regard to the balance of payments problem, including those that suggested the possibility of a "package" approach. Personally, he had been much concerned that this country did not have the wherewithal to continue spending, lending, and investing as it had been doing throughout the world. It seemed vital to world trade in the future that this country's financial markets, which had been developed over a long period of time, not be destroyed by the imposition of selective controls. He would hope that this country's money markets might continue to be available to the world without restriction. If that was to be the case, however, it seemed important that Governmental spending and lending be cut back. The package approach seemed important,

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and it was important for the Federal Reserve System to play its proper role.

Mr. Balderston then referred to the thought expressed by Mr. Deming that once Treasury operations permitted the Open Market Committee might test the effect on interest rates of some mopping up of current liquidity. It seemed to him that there were evidences of "overly excess liquidity," perhaps in the stock market and in the extent of short-term lending abroad. He had no hope that a modest change in the interest rate structure, short or long, would stop the outflow of capital to other countries and the resultant drain on the U. S. gold stock. The rate differential seemed to be too wide. To the extent, however, that American banks were soliciting foreign business, it appeared that some mopping up of liquidity might be worth trying, for he felt fairly sure that there had been a good deal of seepage. Consequently, whenever there was an opportunity, he would like to see an effort to mop up some of the liquidity that seemed to be giving trouble. Then, whenever the Government was prepared to move forward with a package program, the System should be prepared to play its full part.

Turning to the policy directive, Mr. Balderston said he would be inclined to make only necessary changes at this time. He would withhold any overt policy move, such as a change in the discount rate, until a payments crisis was at hand, for he would not want to use ammunition prematurely.

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Chairman Martin commented that this was a relatively easy meeting to summarize. It was clear that the majority of the Committee favored no change in policy at this particular time. He subscribed to that view, but he would like to make certain observations.

He agreed, the Chairman said, with the comments that had been made about the difficulty of obtaining clear perspective, both in terms of the balance of payments and the domestic economy. The outlook was anything but clear. With respect to the comments that had been made about the short-term interest rate, he wished to say that he found this a very confusing area. What impressed him, however, was the number of distortions that were involved when one talked about free markets. There was, for example, the matter of the 4-1/4 per cent interest rate ceiling on financing the Federal debt and what that had done to the debt structure. The success of the Treasury's advance refunding had exceeded his expectations, and it had changed the composition of the Federal debt in a very short period of time. However, the Treasury was now confronted with political uncertainties in regard to the debt ceiling in a peculiarly difficult period. When one used the phrase "free market," allowance had to be made for this kind of distortion and dislocation. Further, while it might be said that there had been free markets, nevertheless there had been discretionary monetary management for many years. These were all factors that must be taken into account.

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With respect to the balance of payments, Chairman Martin said he continued to feel that conditions were gradually moving toward a crisis of some sort. It might not be near at hand; it might be a year or two years in coming. Nevertheless, it seemed to him that present conditions could not continue indefinitely. In his view, too much attention probably was being paid to stimulating the domestic economy through monetary policy and not enough to dealing with the balance of payments. He subscribed to the opinion that the balance of payments problem had become the real shadow over the domestic business scene. The Federal Reserve System, with the regulation of money and credit as its primary responsibility, must evaluate as closely as possible what was involved in the present situation both in respect to the domestic economy and from the standpoint of the balance of payments. The Open Market Committee ought to concentrate on the problem and see if it could not hammer out a policy that would be a little clearer.

There had been references at this meeting to team play and a package deal, Chairman Martin noted. In one sense this was an excellent suggestion, and he would be in favor of it. It should be borne in mind, of course, that the President was more concerned about the balance of payments than almost any other problem. There was no doubt where the President stood, and it should be fully recognized that this problem had been for some time a matter of major concern within the Administration. If the Federal Reserve could mesh in with anything the Administration

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was doing, that would seem very desirable. On the other hand, in talking about team play, it should not be forgotten that most of the time the Federal Reserve, in the field of money and credit, had been considered off the team when it did not do everything that was wanted by the Administration in power. This was a matter of history. Therefore, one must be careful about approaching the idea of team play in the sense of the Federal Reserve wanting to play a leading role or to become the driving force. One must be careful that the Federal Reserve did not get itself into the position of trying to do more than monetary policy should do. As a matter of history, monetary policy had been asked to do too much in the past in handling both inflation and deflation. At the present time, encouragement could be taken from the President's attitude. Everything possible should be done to determine the proper role of the System, both as adviser and in terms of operations.

To that end, the Chairman commented, Mr. Young had put together with the help of staff members of the Board, the New York Bank, and the San Francisco Bank a group of papers that would be distributed today. These papers presented conclusions of the individual authors as to the impact on the domestic economy and on the balance of payments of certain assumed policies, including what he would refer to as a less easy monetary policy, an even less easy policy, and a drastically less easy policy. The papers were intended to be a kind of guide to the Committee members in their thinking on the alternatives that would be available

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if the System was faced with the problem of an international payments crisis.

The Chairman went on to observe that the System, if it did not have the support of the Administration, would be defeated psychologically almost at the start on certain moves that monetary policy could make in relation to the balance of payments problem. It needed the Administration's tacit support. Anything that was done at this juncture ought to be, in that sense, part of a package deal, but the problem should be thought through carefully. For example, in the group of papers that were to be distributed there was one by an individual who took one point of view and another by a person who took the opposite point of view regarding the impact on the balance of payments of a certain move. The papers should not be widely distributed, but the time had come when the Committee should start concentrating on the problem. Perhaps other papers would be developed on the subject. If the System wanted to become part of a team play, those within the System must sharpen their thinking on the impact of various moves. It was with that in mind that the staff documentation had been prepared.

The staff papers referred to by Chairman Martin were then distributed to the members of the Committee.

Turning to today's meeting and monetary policy for the period immediately ahead, the Chairman expressed the view that it would be unwise, from a procedural standpoint, to project shifts in policy within

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an ensuing three-week period even if all of the Committee members were agreed. In his opinion it would be better, if any shift in policy was to be considered, to have another Committee meeting. In other words, it seemed to him undesirable to engineer even modest changes in policy within the period prior to another scheduled meeting. It would be preferable to have another meeting, if necessary, and consider the proposed shift in policy. Generally speaking, he felt that this was the best way for the Committee to operate.

In view of the Treasury's problems, relating to both the debt limit and current and prospective financing, the Chairman expressed the view that the Committee would be pursuing the right course if it maintained virtually the status quo during the next three weeks.

As some of the comments today suggested, Chairman Martin pointed out, the members of the Committee must continue to work on the formulation of the policy directives. As he had said several times, words mean different things to different people around a table. There could hardly be a complete meeting of the minds when certain words were used. As to the formulation of the directive at this meeting, it would appear that the minimum changes would be (1) to eliminate the reference to "substantial" increases in bank credit, money supply, and the reserve base in recent months, and (2) to refer to the implementation of policy "in a period following a major Treasury financing" instead of referring to "the forthcoming Treasury financing." He inquired whether general agreement could be reached on a directive incorporating those minor changes.

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Mr. Bopp stated that he would go along with such a directive if, in the light of the question raised earlier by Mr. Swan, the Account Manager felt that it would be reasonable to call for operations with a view to maintaining about the same degree of firmness in the money market and at the same time to offsetting downward pressures on short-term interest rates.

Mr. Stone indicated that he felt it should be possible to operate satisfactorily under such a directive.

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 execute transactions in the System Open Market Account in accordance with the following current economic policy directive:

It is the Committee's current policy to accommodate moderate growth in bank credit, while aiming at money market conditions that would minimize capital outflows internationally. This policy takes into account the continuing adverse United States balance of payments position and the increases in bank credit, money supply and the reserve base in recent months, but at the same time recognizes the limited progress of the domestic economy, the continuing underutilization of resources, and the absence of general inflationary pressures.

To implement this policy in a period following a major Treasury financing, System open market operations during the next three weeks shall be conducted with a view to maintaining about the same degree of firmness in the money market that has prevailed in recent weeks and to offsetting downward pressures on short-term interest rates, while accommodating moderate reserve expansion.

Votes for this action: Messrs. Martin, Hayes, Balderston, Bopp, Clay, Irons, Mills, Mitchell, Robertson, Scanlon, and Shepardson. Votes against this action: None.

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Chairman Martin noted that the Committee staff had prepared a draft of possible current economic policy directive in the thought that it might form a basis for discussion at this meeting. He would ask the Secretary to distribute copies of the draft directive to the Committee members for their information and review, since it was apparent that the Committee must continue to work on the problem of formulating its directives in the most effective manner.

In distributing copies of the draft directive, Mr. Young commented that whenever there were suggestions for changes in the directive, it might be helpful if the proposed changes were sent to the Secretary in advance of the Committee meeting so that copies of draft directives incorporating such changes could be prepared for distribution to the Committee.

Secretary's Note: In advance of this meeting there had been distributed to the Committee by the Secretary a background statement of current economic position, with the understanding that the statement would be included in the minutes of this meeting. The statement read as follows:

The domestic economic picture reflected several special influences, such as unusually severe winter weather and strikes in some key industries, which added to the low visibility of the statistical readings on the performance of the economy. Most changes in recent weeks, both favorable and unfavorable, have been quite small.

Automobile production and sales remained very high again in February. Retail sales other than automobiles, however, apparently were slightly below their late 1962 record levels in

January and February. Personal income increased in January owing to large veterans payments which more than offset a sizable increase in employee contributions to social insurance and a decline in dividend payments from the unusually high December rate. Aside from these changes, personal income was about the same as in December 1962. The labor market again showed little change, although the seasonally adjusted rate of unemployment edged up in January and again in February.

New orders received by durable goods producers rose appreciably in January to a level slightly above the October 1962 high. Inventory holdings in manufacturing showed no change in January and were only slightly above mid-June 1962. The industrial production index in January was fractionally lower but stayed in the 119 to 120 range it had been in since July 1962.

Consumer prices in January rose very slightly, returning to their November 1962 level; they were 1.4 per cent above a year earlier with food and services mainly responsible. Wholesale commodity prices continued to show little change from the preceding month or from a year earlier.

Yields on corporate bonds showed little change in recent weeks, while on municipal bonds they increased moderately in response to continuing heavy dealer inventories. Yields on Treasury intermediate- and long-term issues also rose somewhat, reflecting Treasury refunding activities. Treasury bill rates dropped slightly below mid-February levels. Yields on mortgages declined a little. Stock market prices declined appreciably during the past two weeks after rising vigorously for more than three months.

Capital market financing by corporations and State and local governments was in moderate volume again in February and is expected to continue moderate in March, especially in the corporate area.

Bank credit rose substantially further in February on a seasonally adjusted basis, reflecting chiefly increases in financial loans and a much smaller than usual decline in holdings of U. S. Government securities. The seasonally adjusted money supply in February apparently was maintained at the daily average level of January, while time and savings deposits increased substantially further. Total reserves and required reserves behind private deposits declined about seasonally over the past four weeks. Free reserves averaged somewhat lower and member bank borrowings higher.

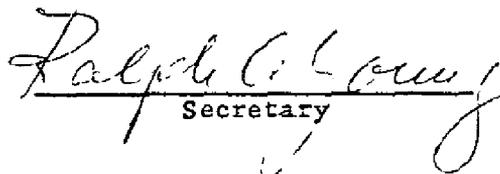
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According to tentative preliminary estimates, the payments deficit was much lower in February than in January. But in view of the influence of the dock strike on trade figures, the average for the past two or three months is more significant than the individual monthly data, and this average shows only a very modest improvement over 1962. The monthly decline in U. S. gold reserves in both January and February was slightly larger than the 1962 average. Exchange markets were generally quiet since the February 12 meeting of the Committee.

It was agreed that the next meeting of the Federal Open Market Committee would be held on Tuesday, March 26, 1963.

The meeting then adjourned.


Secretary