

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, August 7, 1956, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Hayes, Vice Chairman
Mr. Balderston
Mr. Erickson
Mr. Johns
Mr. Mills
Mr. Powell (Part of Meeting)
Mr. Robertson
Mr. Shepardson
Mr. Vardaman
Mr. Fulton, Alternate

Messrs. Bryan, Leedy, Treiber, and Williams,
Alternate Members, Federal Open Market
Committee

Messrs. Leach, Irons, and Mangels, Presidents
of the Federal Reserve Banks of Richmond,
Dallas, and San Francisco, respectively

Mr. E. C. Harris, First Vice President, Federal
Reserve Bank of Chicago

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

Chairman Martin noted that advice had been received of the election of Mr. Hayes as a member and of Mr. Treiber as alternate for Mr.

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Hayes as a member of the Federal Open Market Committee, effective August 1, 1956, to serve for the unexpired portion of the term ending February 28, 1957. Messrs. Hayes and Treiber had taken the oaths of office for their respective positions prior to this meeting.

Chairman Martin suggested that Mr. Hayes be elected Vice Chairman of the Committee succeeding Mr. Sproul, whose resignation became effective June 30, 1956, and Mr. Balderston stated that he would second this proposal.

Thereupon, upon motion duly made and seconded, and by unanimous vote, Mr. Alfred Hayes was elected Vice Chairman of the Federal Open Market Committee, to serve until the election of his successor at the first meeting of the Committee after February 28, 1957, with the understanding in the event of the discontinuance of his official connection with the Federal Reserve Bank of New York he would cease to have any official connection with the Federal Open Market Committee.

In welcoming Mr. Hayes as a member of the Committee, Chairman Martin described the procedure followed in conducting the meetings and their use as a means for discussing all System matters relating to credit policy, with participation including not only Committee members but also the Presidents who were not currently serving as members of the Committee. He emphasized the point that these discussions are for the purpose of giving the different parts of the System the benefit of views of others and that expression of views during such discussions should not be taken as committing a person to any particular view if

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the matter came to a vote.

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the Federal Open Market Committee held on July 17, 1956, were approved.

Before this meeting there had been distributed to the members of the Committee a report covering open market operations during the period July 17 through August 1, 1956, and at this meeting a supplementary report covering commitments executed August 2 through August 6, 1956, was distributed. Copies of both reports have been placed in the files of the Committee.

Upon motion duly made and seconded, and by unanimous vote, the open market transactions during the period July 17 through August 6, 1956, were approved, ratified, and confirmed.

At Chairman Martin's request, Mr. Young made a statement on the economic situation, supplementing the staff memorandum distributed under date of August 3, 1956. He said that the composite of data recently becoming available confirms, as pointed out at the last meeting, that economic activity has resumed an upward slant. Work stoppage for over a month in the steel industry, serious as it has been for activities affected, has not apparently greatly damped expansive trends. Abroad in most industrial countries, output continues at close to record levels. With productive resources in major industrial countries intensively utilized, wage and other costs tending upward, demand pressures strong, and business psychology

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on the buoyant side, pricing conditions in commodity markets in these countries can best be generalized as firm to rising. New international tensions arising out of the Suez Canal incident are a source of fresh uncertainties and, for internationally traded commodities under a strengthening demand situation, have precipitated sharp price increases.

Mr. Young then presented the following comments on specific developments and situations:

(1) Reflecting mainly work stoppages in steel and related industries and some reduction in nondurables output (notably textiles and paperboard), industrial production for July is presently estimated at 135. The index will recover some in August but will not regain its June level because of time necessary to restore full-scale steel output, belated effects on steel consuming industries of short materials and parts supplies, and new work stoppages in the aluminum industry. Increased output of auto parts and equipment for 1957 models is expected to about offset effects on the over-all index of reduced auto assemblies for model changeover.

(2) Construction activity in July, as measured by value put in place, was at a record high and 3 per cent above a year earlier. The advance reflected especially increased outlays for industrial construction and some further rise for commercial building. Residential and public construction were about maintained.

(3) Employment in mid-July showed maintenance of record job levels, so that little change was registered in unemployment figures, which exclude for the most part workers on strike. Unemployment claims for the last week of July totaled 1.2 million, up 140,000 from last year, mainly reflecting layoffs in the automobile and related industries.

(4) Personal incomes in June showed a further moderate increase, reaching a record annual rate of \$324 billion, up \$7 billion from the end of year and \$18 billion over a year ago. The wage component of personal income, which accounts for nearly 70 per cent of the total, is currently under upward push from wage

rate adjustments in the steel and aluminum industries and from automatic cost of living adjustments affecting before long possibly a million workers.

(5) Reflecting rising disposable incomes, consumer takings at retail continued strong in June and at department stores in July. Passenger car sales, in the first 20 days of July, new and used, were off from June, but only by about the usual seasonal amount. With new model shutdowns approaching, this encouraged manufacturers to maintain or increase assemblies moderately. New and used car inventories about held even. Judging from department store figures, sales of household durables in July continued to show strength, although sales of major appliances were off from their high year-ago volume.

(6) The rate of instalment credit expansion, seasonally adjusted, slackened further in June and probably also again in July. This slackening, as in other recent months, reflects an overtaking of new extensions of credit by the steady climb of repayments on previously incurred debts. While further liberalization of downpayment terms in instalment financing has apparently been checked, available information suggests that the proportion of credit written on very liberal terms has continued to rise.

(7) Manufacturers' sales in June held close to record May levels, and, while new orders were off, they continued to exceed sales, thus adding further to unfilled orders. Inventories at manufacturing levels extended their rise, with the increase concentrated in nondurable lines, but distributive inventories, especially at retail, were off some. Thus, the total rise in business inventories was probably less than in other recent months. The work-off of steel inventories at the manufacturing level in July, with relatively small change in distributive inventory positions, is expected to result in some decline in the over-all business inventory position for this month.

(8) At wholesale, prices of industrial materials, especially metals and rubber, have recently moved upward, some of them influenced by the Suez Canal crisis. Lumber and plywood have weakened some from earlier in the year and textiles fibres other than wool have continued on the soft side. In steel, smaller producers who continued in operations and steel warehouses have advanced prices by an average of about \$10 a ton, slightly more than the \$8.50 increase announced yesterday by the major producer. Since mid-July a number of producers of finished metal products and of tires have raised their prices.

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(9) Average prices of farm products have changed little in the past two months after advancing 10 per cent from December to mid-June. Recently meat prices have moved up sharply and grains have advanced some. Cotton, however, has declined over the past month to about the level of the new crop future. Fruits, vegetables, fats and oils have declined moderately.

(10) Consumer prices at mid-June were 1.5 per cent higher than a year ago, most of the rise occurring in May and June. Judging from recent retail price tendencies for food, services, and rents, a further advance for consumer prices seems likely to mid-July.

(11) Reflecting the strong international situation, U. S. exports showed a marked rise in June. Exports of non-agricultural products rose very sharply, and a further advance was registered for agricultural exports.

(12) Abroad in industrial countries, heavy capital investment by business enterprise continues to provide a major expansive impulse. The latest plant and equipment surveys conducted this spring in such countries as Canada, Britain, and Sweden all show substantial upward revisions from similar surveys made last fall. The French economy is under special pressure because of the drain on resources resulting from military operations in Algeria.

In concluding his presentation, Mr. Young suggested that a special comment might be in order. With intensive utilization of available resources in this country and with its aggregate demand resuming expansive tendencies, he said, price strength in many markets and upward price pressures in other markets are to be expected. In a limited business cycle sense, these price characteristics may be called inflationary. They are not inflationary, however, in the sense that they result from lax or irresponsible financial policy--fiscal and monetary--on the part of the Governmental authorities. The problem faced by the economy at this time is not inflation fed in this way, Mr. Young said, but rather inflation fed by the competitive spending, investing, and

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borrowing propensities of a highly optimistic business and consumer public. The dangers are in misdirected use of resources, unwise judgment as to business and investment opportunity, overoptimism as to management's ability to pass along higher wages and other costs into higher prices, overcommitment of credit based on a discounting of the future that is too favorable to the present, and a cumulative deterioration in the quality of credit. At this stage of a very long business upswing--interrupted by only two minor cyclical setbacks, and at the present high level of commodity prices--established as a result of war, postwar, and post-Korean monetary and fiscal inflations, these dangers are very real. The practical challenge to monetary policy at this phase, Mr. Young said, is to minimize the dangers by fostering as economical or efficient an allocation of scarce resources, including savings, as can reasonably be effected by market processes.

Chairman Martin next called upon Mr. Thomas, who commented on credit developments as follows:

Credit developments in the last three weeks have not been particularly striking, reflecting the summer lull. Comparisons with previous years are vitiated by the deferment of the midsummer Treasury cash financing to a later date than usual this year. The most striking developments were sharp decreases in bank deposits and loans at New York City and Chicago banks, in contrast to relatively little change at banks in other leading cities. Commercial loans declined moderately in July, and loans on securities and holdings of securities also declined. The total money supply is estimated to have shown a small further increase on a seasonally adjusted basis in July, although less than in July of 1955.

Capital market offerings, which were very large in July, are expected to be more moderate in August but may exceed the total for August of any previous year. Reports

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continue to indicate a large volume of issues in prospect, including both public offerings and private placements. Some of the proceeds of issues by finance companies may be used to pay off bank loans. There are indications that some of the corporate demand for bank loans is for relatively long terms and for capital purposes. State and local Government financing is expected to be fairly moderate in August which will help dealers lighten heavy inventories, but large offerings are in prospect for the fall months.

The demands on the capital markets have been reflected in a further rise in corporate bond yields to new highs on both outstanding securities and new issues. Yields on Treasury bonds, which declined in May and June, have again risen to or above previous highs for this year and are close to 1953 highs. Stock prices have generally been close to highs of the year. Yesterday's sharp drop may reflect in part a technical reaction. In contrast to bond yields, Treasury bill yields have continued relatively low, reflecting strong demand for liquidity instruments at a time when they were in reduced supply and the low level of net borrowed reserves, which reduced pressures on banks as compared with last spring.

The Treasury's offering of \$3 billion of 2-3/4 per cent tax anticipation certificates maturing next March will provide an additional supply of short-term securities and may relieve some of the demand pressures, although two-thirds of the proceeds will be used to retire debt. This offering apparently has been popular in contrast to the earlier exchange offering of some \$12 billion of one-year-plus notes at 2-3/4 per cent, on which attrition totaled almost \$900 million. The Treasury may need to borrow an additional \$2 or \$3 billion of cash toward the end of October.

Looking ahead, rough estimates of capital and credit needs that would be consistent with relatively full and sustained employment without inflation, indicate that credit growth during the remainder of this year should be less than last year. However, reports indicate continued strong demands. Banks are reported to be considering a further rise in the prime rate and also are considering stricter requirements as to maintenance of minimum balances, as well as limitation of the prime rate to a smaller group of borrowers. In this situation, particularly in view of recent upward pressures on commodity prices, it would seem that borrowers should be forced to endeavor to raise funds from savings before resorting to bank credit and that there should be continued limitation of credit and monetary expansion to a very moderate rate. There seems to be a general recognition and expectation in financial circles of the need

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for tight money. Last fall, banks found it necessary to keep their borrowings at a relatively high level--\$800 million to \$1.1 billion--and System open market operations were moderate and were used mostly in periods of particularly heavy needs. Policy questions before the Committee at this time are whether operations should be directed toward maintaining some predetermined level of net borrowed reserves and, if so, at what level; or, should purchases except those to moderate temporary wide swings, be held off until clearly needed to relieve undue pressures?

In response to a question from Mr. Harris, Chairman Martin stated that he thought the suggestion that the Treasury might issue additional bills to take care of investor demand for short-term securities was still under consideration and that there was a possibility that such an offering would be made.

Chairman Martin then called upon Mr. Hayes, who made a statement substantially as follows:

1. For several months there has been a close balance between the forces of inflation and deflation, but settlement of the steel strike appears to have tipped the balance in favor of the former. The sizeable increases in steel workers' wages and steel prices are likely to start a chain reaction in other industries. Already there is some evidence that this is taking place.

2. Even before settlement of the steel strike there were signs of increasing confidence in the business outlook. The so-called "weak spots," especially automobiles and housing, appear at least to have stabilized, while some of the "strong spots" seem stronger than ever.

3. Consumer demand is high; business and public capital outlays are very large; total employment recently attained a new high. Residential construction, while well below last year's record, is still at a very satisfactory level if viewed in longer perspective. Excess dealers' stocks of automobiles are being liquidated.

4. Prices in many areas seem to confirm a tendency for effective demand to outrun available resources. In June, the consumer price index rose to a new high record, and a further increase is probable. Price rises in basic materials will

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soon be reflected in higher prices of finished goods, some of which have already appeared.

5. Long-term interest rates are under pressure. The market apparently expects heavy demands for capital and credit.

6. Demand for bank credit was very strong in the first half of the year. While it may be not quite so strong in the second half, after allowing for seasonal influences it will doubtless still be very substantial. The seasonal expansion in loans should be under way within a month.

7. The business and credit situation calls for a policy of restraint on the part of the Federal Reserve. We shall of course wish to make reserves available to meet seasonal requirements and the basic need of long-term growth. The System made it clear in June that it was prepared to supply sufficient reserves to avoid a severe credit squeeze. Gross member bank borrowings recently have been around the \$700 million mark.

8. Under present conditions, with inflationary pressures growing, reserves for seasonal needs should be provided only as the needs occur. To provide them in advance of needs might cause confusion, create easier money market conditions, and tend to encourage a too rapid expansion of bank credit.

9. The Treasury closed its books last night on its cash offering of \$3 billion tax anticipation certificates, to be paid for August 15. In view of the Treasury financing, we should try to maintain an even keel in the money market and credit conditions for the next couple of weeks. Thereafter, assuming that business conditions continue in accordance with expectations, we may need to move toward more restraint.

10. Recognizing that "net borrowed reserves" are not an infallible measure of credit restraint, we should nevertheless seek to keep them at a level of about a quarter of a billion dollars through completion of the Treasury financing--thereafter trending upward and perhaps reaching \$400 million during the subsequent two weeks.

11. Since May 23, 1956, the general directive from the Committee to the New York Bank has directed open market transactions with a view to "restraining inflationary developments in the interest of sustainable growth, while taking into account any deflationary tendencies in the economy." Since the balance of influences in the economy is now clearly on the side of expansion and possibly inflation, we should consider the desirability of dropping the clause "while taking into account any deflationary tendencies in the economy."

12. The tense and unpredictable situation in the Middle East suggests that any changes in credit policy should be decidedly cautious until that situation has been further clarified.

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13. The officers of the New York Bank believe that there should be no change at this time in the Bank's discount rate. We should be alert to the possibility of increasing the rate within the next month or so if conditions then warrant it. Incidentally, a few of the directors at the last board meeting of the Bank spoke of this possibility.

Mr. Johns said that he and others at the St. Louis Bank had been considering and debating the problems stated by Mr. Young at the conclusion of his presentation and the questions posed by Mr. Thomas at the end of his presentation. This group, which includes members of the Board of Directors who serve on the executive committee of the St. Louis Bank, doubts whether in the present situation there may not be danger that the monetary authorities might attempt to do more than they can reasonably be expected to do and to assume more responsibility than really belongs to them. That, however, does not say that the monetary authorities should not do what they reasonably can do. Therefore, Mr. Johns said, his group was inclined to agree with the position stated by Mr. Hayes, namely, that in the period between this and its next meeting the Committee should have a target range for net borrowed reserves around the \$400 million mark, although it should not move too quickly to that figure in view of the payment to be made shortly for the current Treasury offering. At the moment, Mr. Johns said, the St. Louis Bank contemplates no change in its discount rate.

Mr. Bryan reported some feeling at the Atlanta Bank that the recent wage increases do not necessarily lead to as much inflation as we might think. However, that view rests upon certain hypotheses as

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to future behavior of the economy and whether, in the business cycle, these price increases produce unemployment and other developments that would be as undesirable as inflation. The general assumption at Atlanta, Mr. Bryan said, was that the economy needs restraint at the present time. The problem is how to apply that restraint in terms of magnitude and instruments to be used, Mr. Bryan said; should reserves first be supplied through the open market only when clearly needed and for the purpose of relieving evidences of disorder in the capital markets, to be followed by an increase in the discount rate; or should the System flag down the economy soon with an increase in the discount rate and then use open market operations? Mr. Bryan said that he was inclined to supply reserves in a niggardly way through the open market and then to increase the discount rate, although it might be well to tell the banking system promptly that it should be reluctant in making commitments for fall borrowing.

Mr. Williams described economic activity in the Philadelphia District as continuing at a high level, despite some soft spots. Resort business this summer has not lived up to earlier expectations although there is optimism concerning August and part of September. Agriculture is one of the soft spots. On the whole, however, the economy is operating at a high level. Loans at banks increased slightly last week after a mild decline over the preceding five weeks. Mr. Williams said there is some evidence that the small growth in deposits in the Philadelphia

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area is in part the result of the small balances maintained by borrowers located outside the area, and banks are considering ways of bringing about a more desirable relationship in this respect. Some banks are clearly pessimistic about meeting loan demands without borrowing, Mr. Williams said, and this leaves the Reserve Bank with the prospect of a continued discount problem. The banks are sensitive to this situation and have had discussions with selected large corporate borrowers and put them on notice regarding the restrictive policy they expect to follow regarding loan extensions during the fall months. The general approach the Philadelphia Bank is taking to the discount problem, Mr. Williams said, is to continue to discuss it with the banks. The spirit of the Reserve Bank's approach, he said, was constructive restraint. The banks seem to expect that the Reserve Bank will move before too long to a higher discount rate.

Mr. Fulton said that, with wage settlements having been made by several key industries of the Cleveland District, with substantial increases, and with the coal settlement coming up, he anticipated a surge of business rather than any hesitancy. The price increase announced for steel was smaller than expected but would result in a substantial increase in costs for users of steel, and they would also have increased labor costs. For some time, Mr. Fulton said, he had felt the Committee's policy had not been sufficiently restrictive to

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contain the pressures building up in the economy. He felt it would be only a short time until a rise in the discount rate would be completely appropriate. In the meantime, there should be no slack in the money market and net borrowed reserves should be higher than they have been for some time. Mr. Fulton said that he agreed with Mr. Hayes that the Committee should look forward in the reasonably near future to taking such steps as will dampen the inflation which is not only in the making but which is actively in operation.

Mr. Shepardson said that everything pointed to further pressures on the upward side, even more definitely than the Committee had been thinking in the past few weeks, and we should be in the position of exercising further restraint for the period immediately ahead. Apparently it would be desirable to hold the present situation through the Treasury financing, but his hope would be that the Committee would be as quick to take up any unexpected slack as it had been to take up unexpected tightness. It was Mr. Shepardson's view that, since the last meeting at which the emphasis in discussion was on the side of tightness, the operation of the System account had tended to let developments toward ease run, while it had been quick to offset any developments toward tightness. He hoped that the Committee could begin to tighten the situation as it approached an expansion period around the beginning of next month. Mr. Shepardson said that he also felt that toward the end of this month or early in September it would be appropriate to increase the discount rate.

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Mr. Robertson stated that, in line with what had been said this morning, he felt that for the future the Committee should employ a greater amount of restrictiveness. It should not credit monetary policy for keeping an even keel when things go well and deny responsibility when inflationary pressures seem to get the upper hand. Mr. Robertson said he agreed with Mr. Hayes that the reference to taking account of deflationary tendencies should be deleted from clause (b) of the first paragraph of the Committee's directive to the New York Bank. He would disagree with Mr. Bryan that open market operations should be used to take the load of restriction first, and let the discount rate take second place, his feeling being that the time is rapidly approaching when the Reserve Banks should consider increasing discount rates. Mr. Robertson said that it seemed clear that everyone who had commented thus far at the meeting agreed that the battle for the next few months was one of fighting inflation and that the System should do it with every possible tool that it had. He would be reluctant in adding reserves through open market operations and would take advantage of every opportunity to tighten the situation, moving in one direction. He would not set any goal for negative free reserves but would hope that they would move upwards.

Mr. Mills then made a statement substantially as follows:

I am disturbed by the policy recommendations that have been made against the background of the inflationary factors foreseen by Mr. Young and Mr. Thomas in their discussion of the economic situation. Adoption of these recommendations

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under present tight money conditions would, in my opinion, compel a continuance of the contraction in bank loans and investments that has gone on for some time in the face of a substantially lower level of negative free reserves than was the case earlier this year, and obviously would not provide for the seasonal expansion of bank credit for which we have previously agreed to supply reserves. A 2-3/4 per cent rate for Federal funds and a relatively high volume of Federal Reserve Bank discounts give evidence of tight money conditions. A still better indicator of tightness, that opposes the superficial evidence of ease implied by the reduction in negative free reserves, is the constant use week after week of around \$1-1/2 billion of funds borrowed by the reporting member banks from the Federal Reserve Banks and from others. If new reserves had really become available in quantity, it is certain that bank loans and investments would not have fallen and banks would have had less need for borrowed funds.

In short, the type of policy that is favored would force a further contraction of bank credit just at the time seasonal demands for credit must be met through reserve support. Moreover, such a policy would tend to induce added weakness in the prices for long-term U. S. Government securities when investor confidence may already be unsettled by the international tensions resulting from the Suez Canal crisis. Everything considered, it seems to me that action taken now to help stabilize the market for long-term U. S. Government securities would bolster investor confidence at the same time the System was supplying reserves in acknowledgment of its declared commitment to meet the legitimate needs of the commercial banks.

Therefore, it is recommended that the System open market account make direct purchases of Treasury bills during the next week or ten days amounting to \$100 million, to the end of relieving the pressure on the commercial banks to liquidate U. S. Government securities and in the process to help stabilize their market. Such action would also avoid depending excessively on the estimated expansion of float for supplying the reserves that will be needed to prevent the prospective increase on August 15 in bank Tax and Loan Account deposits from causing undue tightness. It is my opinion that we should be wary of adopting any policy at this time that would pass from desirable restraint into a policy of credit restriction.

Mr. Vardaman stated that, in principle, his remarks would be repetitive of those by Messrs. Hayes and Johns except that he did not

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interpret their remarks to mean what Mr. Mills apparently had interpreted them to mean. He would not interpret those remarks to advocate credit contraction or to advocate undue credit restriction as compared with a policy of normal or what we believe to be sound credit restraint. Mr. Vardaman said there would be danger if there were any possibility that Federal Reserve credit policy would be interpreted to mean contraction; this would be extremely bad and he could not go along with any such policy. His view was that the System should pursue a policy that could only be interpreted as one of gentle restraint until such time as further restraint may become necessary. He would not recommend an increase in discount rates now, feeling that to the uninitiated such an increase might be interpreted as a further spread of the price rise that might be a result of the steel wage settlement. An increase in the cost of money in the short-term range is not restrictive, Mr. Vardaman said. Continuance of a quarter of a billion of negative free reserves possibly could be followed, if necessary as conditions warranted, by an increase up to \$400 million or even \$500 million. As to the Committee's directive, Mr. Vardaman said that rather than delete the reference to taking account of deflationary conditions, he had thought that clause (b) of the first paragraph of the Committee's directive might be changed by adding words which would make that part read "...while taking into account any deflationary tendencies WHICH MIGHT DEVELOP in the economy."

Mr. Hayes said that he would like to make it clear that he

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did not intend and he did not believe the others commenting intended to imply that the System would not supply sufficient reserves to the market to take care of a good part of the credit expansion that was expected and which it was realized was inevitable during the remainder of this year. He expected an increase in loans and that the System would have to provide a good part of the reserves for that increase. Mr. Hayes' point was that, rather than provide such reserves now or in the near future, the System should "lean back a little" and only put them out grudgingly.

Chairman Martin stated that he thought this was a desirable clarification, and he then called upon Mr. Leach.

Mr. Leach reported scattered evidence of increasing strength in the economy of the Fifth District. During July there was little change in total loans of reporting member banks in the district or in member bank borrowings from the Reserve Bank. Member banks have indicated that loan demand continues strong and that it is expected to be stronger. One type of business loan demand that is expanding rapidly comes from dealers in road building machinery. Several of the larger banks pointed out to him yesterday, Mr. Leach said, that substantial seasonal increases in loan demand were expected on top of a base already extremely high. The banks know that they will have to make seasonal loans from now on during most of the rest of this year. Bankers say that they are screening loans closely and are turning down requests for term loans among others. Despite this

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screening, unwanted new loan peaks are expected. Mr. Leach suggested that the combination of increasing loan demand and of increases in depreciation in the securities accounts of banks is likely to produce increased problems in loan administration at the Reserve Banks, especially with respect to those member banks that have been borrowing rather steadily. In commenting on policy to be followed, Mr. Leach recalled that at the preceding meeting he expressed the view that the Committee should hold a tight rein on credit. Developments since that time have caused him to think that policy should be somewhat tighter after the conclusion of the current Treasury financing. This would presumably, but not necessarily, mean net borrowed reserves in the \$300 to \$400 million area. If inflationary pressures accelerate, as he thinks they will, Mr. Leach said he would not like to see the System lag in taking additional restrictive measures. At the moment, however, he would not recommend an increase in the discount rate of the Richmond Bank. He would delete that part of clause (b) in the first paragraph of the Committee's directive which provides that the agent Bank take into account deflationary tendencies in the economy. Responding to a comment by Mr. Robertson on the larger expansion in bank loans this year than last, Mr. Leach said that banks are quite aware of the increase that has taken place in loans, that they are concerned about it, and that because of their concern the System need not tell them that they should be screening loans now.

Mr. Leedy said that signs of inflation were flying in the air and that he thought they had become increasingly apparent in the past

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six weeks. Six weeks ago, at least some members of the Committee felt that, during the period of the Treasury's financing, it was necessary to be cautious in carrying on the Committee's restrictive policy. Three weeks ago, because of the expected Treasury cash financing and the steel strike, there was a feeling that the Committee should proceed with considerable caution. Looking ahead, the System should of course take account of the Treasury's needs. Also, it must note developments in the Suez area. However, Mr. Leedy's view was that in the light of information before it the Committee should attempt to move further in the direction of applying restraint. He would concur with the view expressed by Mr. Hayes that over the period of the next two weeks the Committee should attempt to maintain stability and he would suggest a net borrowed reserve level around \$250 million, the same as the target discussed at the meeting three weeks ago. After that, barring unforeseen events, he would move in the direction of tightening reserves. Noting his concern with the agricultural situation, particularly its importance to the Tenth District, Mr. Leedy said that the most important need for agriculture was that it have a healthy economy into which it could move its products. Since the over-all situation did not now call for taking account of deflationary tendencies in the economy, Mr. Leedy said that he, too, would remove from the Committee's directive the clause to which Mr. Hayes and others had referred. He would postpone action on the discount rate until after there had been an opportunity to use

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open market operations to bring about some increase in restraint.

Mr. Powell, whose train had been delayed in reaching Washington this morning, entered the meeting during Mr. Leedy's statement.

Mr. Harris stated that retail sales in the Chicago District were holding steady at high levels; sales at department stores and appliance stores during July were ahead of the excellent results a year earlier. Price increases have been announced recently by manufacturers of a considerable number of items including nearly all consumer durables other than automobiles. Consumers are being urged by some retailers and advisory services to "buy before prices rise." Employment is somewhat above last year in virtually all Seventh District cities except those concentrating on automobiles and farm machinery. One large farm machinery manufacturer has announced plans for additional layoffs. Three other firms are exploring merger possibilities. Aside from automobile and farm machinery, the prospect is for a further rise in hirings in the next few weeks. The steel strike has had little effect on employment or output except in closely related mining and transportation. Steel consuming industries have reported no significant layoffs, although some layoffs are expected before steel output is back to capacity and the supply lines get fully replenished. Conditions in agriculture continue at the improved level noted at midyear but there is no evidence yet of a pickup in farmer purchases. Construction contract awards were about the same during the first half of this year

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as in the corresponding period of 1955, although there was a slump in June. The residential segment has been the weak part of construction with most other types showing increases this year. Residential mortgage money is tighter than last year and rates are up a quarter to one-half per cent on conventional mortgages. Lenders express no dissatisfaction with the credit situation on either new or used houses and have stated that they are getting enough credit to take care of transactions. Business loan demand is expected to continue at a high level and to provide a larger than seasonal rise during the rest of this year unless restrained by monetary action. Seasonal loan expansion will automatically take care of some tightening. As to the Committee's course of action, Mr. Harris said that he would like to see the net borrowed reserve picture tighten up somewhat above the \$250 million level. He felt that an increase in discount rate would be a rather dramatic change that might have repercussions and it did not seem to him that the situation now warranted such action, although three weeks from now it might be considered.

Mr. Powell said that conditions in the Ninth District are slipping a little; retail trade is not as buoyant as in earlier reports this year and is barely holding level with last year's figures. Industrial employment is very full and unemployment is very low. Construction contract awards have fallen off, both residential and nonresidential, and it appears that the building boom is flattening out, although some architects continue to say that they

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have more work on their drawing boards than ever before. Automobile sales have been good and dealers' stocks of 1956 models have been worked down from burdensome levels to the point where there may be a shortage of new cars in dealers' inventories by the time 1957 models are introduced. Crop prospects have been hurt by excessive rain. Mr. Powell said that he could see no reason for not maintaining a credit restraint policy, although under certain conditions it might be necessary to relax controls in a rapid and dramatic form. He referred to the conditions in the Suez area. As to the discount rate, Mr. Powell stated that the directors of the Minneapolis Bank had come to feel that that district should no longer be a "stalking horse" for the 3 per cent rate, and that unless some other districts came up to that rate soon they might act to reduce it to the level that prevailed generally at other Reserve Banks, inasmuch as the Ninth District did not call for a higher rate than other parts of the country.

Mr. Mangels referred to his comments on the discount rate at the two preceding meetings to the effect that while the San Francisco Bank had maintained the 3 per cent rate, there had been some difference of opinion among the directors as to whether it should have been reduced to the level that prevailed at most Reserve Banks. Another meeting of the directors would be held tomorrow at which time he expected to recommend maintenance of the 3 per cent rate. Mr. Mangels said he thought the 3 per cent rate would be continued and that on the

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basis of the Twelfth District economy, the Bank had been right in having this rate. Mr. Mangels described continuing expansion in Twelfth District business activity, including moderate increases in retail sales and employment. Total construction is about the same as a year ago, residential building having declined and other construction having increased. The automobile situation has improved quite materially and June sales in California, on the basis of preliminary estimates, have been running about 10 per cent ahead of May, with reports of isolated instances in which dealers were running out of stocks of 1956 models and were going to the Midwest to obtain additional cars prior to introduction of 1957 models. Prices of new and used cars have improved. Bank loans at Twelfth District banks have continued to increase and Mr. Mangels presented detailed comparisons of changes in the Twelfth District in relation to changes in the United States as a whole. The cash position of Twelfth District banks is good and borrowings at the Reserve Bank last Friday were only \$5 million. At that time, two country banks were borrowing to meet seasonal agricultural needs and one city bank that has been a consistent borrower this year was borrowing. Reporting member banks indicate total borrowings of about \$225 million including Federal funds and sales of Federal funds and loans to banks of about \$304 million. Bankers feel that business is quite good, Mr. Mangels said, and they are looking forward to a further increase during the fourth quarter of the year. They are continuing to screen loans quite carefully but that is a result of policy rather than a lack of lendable

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funds. Mr. Mangels expressed the view that the System was at a point where it could begin to tighten up somewhat and he had in mind net borrowed reserves somewhere in the \$300 million area, over or under, preferably on the over side. He would favor a change in the directive to omit reference to deflationary factors.

Mr. Mangels referred to the comments made by Mr. Johns at two recent meetings regarding the possibility of a reduction in reserve requirements and stated that, following the last meeting, he requested his Bank's Research Department to check information as to what the result would be if reserve requirements were reduced by, say, 1 per cent and float were reduced as an offset by an increase in the maximum deferred availability schedule to three days. Mr. Mangels commented on various sets of figures that would result from reductions in reserve requirements and an increase in the time schedule. It was his thought that a study of float along these lines might be of interest to the Committee or to the Presidents' Conference.

Mr. Irons said that conditions in the Dallas District are strong and that such changes as have occurred recently have been largely seasonal in nature. Employment is high and the labor market is tight. The steel strike has not continued long enough to cause problems in the Dallas District. Construction, particularly non-residential, is running at a very high level. The petroleum industry

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also is operating at a very high level and the outlook is strong. Agriculture is feeling the continued drought with some parts of the Dallas District suffering from extreme dryness. Generally, however, conditions are very strong and attitudes are quite optimistic. Mr. Irons said that bank loans have tended to level off at peak levels and that he believed there was a little less pressure on banks than two or three months ago. Borrowings from the Reserve Bank have been somewhat lower and range in the \$18 to \$20 million area, in contrast with \$40 to \$50 million a few months ago. Only four or five country banks are borrowing and those borrowings are strictly for seasonal needs. Country banks generally have excess free reserves.

As to policy, Mr. Irons said that on the basis of conditions in the Dallas District and the national picture as he saw it, he would concur in the suggestion for eliminating from clause (b) of the Committee's directive the statement that it should now take into account deflationary tendencies. He felt that policy should be toward firmer conditions than have existed recently in the money market. Recent operations seem to have tended on the side of ease at times, and he would lean to a firmer policy. This would still be consistent with supplying seasonal requirements, Mr. Irons said, although he would not be averse to seeing an increase in the volume of discounts. As far as the discount rate is concerned, Mr. Irons said that his Bank would not have a meeting of directors during August but he felt that the System should be preparing to move toward the 3 per cent rate

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now existing at two Banks. This would not be a startling or shock treatment but was rather expected at this time, he said, and with money market conditions as they are, there would be surprise if the System did not move in that direction. Summing up, Mr. Irons said he would not favor a sharp or dramatic move, but he hoped that policy would tend on the side of firmness and he would favor an increase in the discount rate within the next month and would not consider this to be a drastic action.

Mr. Erickson said that conditions in the Boston District still remained very strong. Nonagricultural employment in June was the second best in the postwar period. Construction contract awards apparently are running better than in the rest of the country, a 15 per cent increase for the first 22 days of July over last year having followed a 41 per cent increase in June over June 1955. Even residential building had shown an increase. Deposits at mutual savings banks on June 30 were over 7 per cent higher than a year ago. Loan demand is still quite strong, although reporting member banks are not quite up to their peaks. The discount window of the Boston Bank is not being used to quite the extent that it was earlier this year. Sentiment throughout the district is very strong, Mr. Erickson said, and the inflationary forces seem to be gathering. He felt the Committee should lean against that tendency more than it has. It should delete from its directive to the New York Bank the instruction to take account of deflationary forces. He would not recommend an increase in

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the discount rate during the next three weeks but would consider very seriously such an increase in September. Net borrowed reserves should remain near the present level until the Treasury financing is out of the way and should then be increased. He would not set any figure but would tend in that direction, depending on the market.

Mr. Balderston said the situation seemed to be one calling for a continuation of the existing degree of tightness for the next three weeks. However, he hoped that the interval would be used for consideration throughout the System of a later increase in the discount rate so that the System might control the availability of credit through a rise in its price as well as by restraint on its volume. There are two reasons for maintaining the present level of tightness for the moment, he said, one being the desire to maintain an even keel until the current Treasury financing is completed, the other being to wait until developments in the Middle East are a little clearer. If the passage of tankers through the Suez Canal is interrupted, the amount of oil available to Britain and Western Europe might be reduced by 50 per cent and result in lessening the oil available in the United States.

If loan demand continues and if the demand for capital is maintained, there will be a tendency toward increased prices. Mr. Balderston said that it seemed to him that the steel strike settlement posed afresh the problem of the wage-price spiral and of the

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dilemma of unemployment versus inflation. If the rise in steel prices could be looked upon as a temporary offset to increased costs, it would not be so serious. However, he anticipated that it would tend to be permanent, both for steel itself and for fabricated steel products. Mr. Balderston said that he would concur in Mr. Hayes' suggestion that the Committee change its current directive by deleting the instruction to take account of deflationary forces, and he said that he hoped the System would be prepared to move at an appropriate time, perhaps later this month, with respect to an increase in the discount rate and toward some further restraint upon the volume of credit. He felt that the time has come to resist the inching up of prices that we have seen for a year. Mr. Balderston also referred to the comment Mr. Johns had made regarding the views of some of the directors of the St. Louis Bank that monetary authorities should not take on more responsibility than they could carry for controlling the wage-cost spiral. He expressed the view that this sounded like defeatism.

Mr. Shepardson noted that several comments had been made about the agricultural situation, and he stated that he wished to emphasize that in general the agricultural situation is much improved in comparison with what it was earlier this year. The pig crop is down and there will be less pork coming onto the market during the latter part of this year. Fewer cattle are on feed and there will be less heavy beef on the market later this year. While the drought situation is

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critical in some areas, nothing can help that situation much except some rain. One exception to the latter statement, Mr. Shepardson said, was the hope that the soil bank would serve as insurance; some eleven million acres have been signed up thus far under the program, which will call for Soil Bank payments of some \$225 million. Much of this represents relief to farmers faced with crop failure. Mr. Shepardson recognized that there were still small uneconomic farm units that were not doing well and that inevitably could not do well, but he said on the whole the agricultural situation at the present time is showing some improvement.

Mr. Johns referred to the comment made by Mr. Balderston as to his (Mr. Johns) report of the attitude of some directors of the St. Louis Bank and said that he would like to restate his earlier comment. The directors to whom he referred contemplated the possibility that, if the Federal Reserve were to undertake full responsibility for halting the inflationary pressures resulting from the wage-price-cost squeeze, its actions might bring about the kind of situation that Mr. Mills had spoken of and might bring economic activity to a grinding halt. The directors would not wish to do that, but they still held the view that the System should do what it appropriately could do to control this situation without bringing about any such catastrophic result. Just how this would be done was the question. While his directors would not wish to grind the economy to a halt, Mr. Johns said that they and banks generally would be surprised if the System

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did not exercise greater restraint.

Chairman Martin said that he thought it very appropriate to bring out the idea that we should not try to do more with monetary and credit policy than can be done with that instrument. He felt that the discussion at this meeting had been useful and that it pointed up the critical problems the System was facing. The System should be very careful about projecting the future too positively, but it should not be afraid to take cognizance of signs that are perfectly clear. It should keep flexible. It should not move to a position and say, "here we stand." That flexible approach is the one the Committee has been trying to pursue.

Chairman Martin went on to say that it seemed to him that all the signs are tending in the direction that Mr. Young indicated in the closing statement he made. While he had not read this statement before, he felt that it brought out the elements of the problems that the Committee had had before it over the past year or so. This could be looked upon as a testing period, and there would be increased problems ahead. The Suez problem is one that should not be ignored by the Committee, but that problem should not lead it from a course of action which the monetary authority should adopt in terms of the over-all economy and which it should continually review as developments take place at Suez. The existence of the Suez problem should not cause the Committee to delay and delay actions which the evidence suggested should be taken in dealing with the problems before it.

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The wage-cost spiral needs no comment, Chairman Martin said. He felt in fact that we were bordering on a state of over-employment, the same type of over-employment that had developed in some foreign countries. For example, he had noted in Chicago last week in a small area near the railroad station a great many "help wanted" signs. This "straw" was indicative, for during the summer period normally a let-down in demand for help in an area adjacent to the railroads could be expected. The Chairman said that, as he had indicated before, he felt the steel strike had been a disaster and that it had caused the problems of the System and of the economy to become much more difficult, notwithstanding the reductions that had taken place in steel inventories. Actually, imbalance in inventories for the economy as a whole had been deepened by the steel strike. He felt that some of the comments of persons in the steel industry had been misleading. Chairman Martin said that residential building could be expected to decline in the last half of the year and he hoped it would do so. If residential building and automobile production do not decline during the second half of this year, he did not see how other demand could be taken care of. In his discussions with automobile company executives within the last few days, he found they were not nearly as pessimistic as they were a couple of months ago and that, in terms of anticipated production during the last quarter of the year, they might repeat the mistake they made a year ago of increasing production schedules to a point that would create a 1957 situation that was very difficult to

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deal with. He hoped this would not be the case and he was not intending to reflect on the managements of the automobile companies, but the attitude that had been revealed had frightened him. In addition to that, plans for new plant and equipment plus the psychology of inflation should not be turned aside.

Chairman Martin said that he did not know how much the System could do to deal with these forces but that it should be doing whatever it could. It probably would be roundly criticized for such action, which would come at an unfortunate time in many respects. However, plant and equipment expenditures should not be financed out of bank credit and the Committee should not ignore that fact. It was dealing with an imbalance in supply of goods that could lead to a world debacle of the same type that was experienced in 1929. The time to be talking about that problem is now and not after the debacle has come. At that time, we would have to be talking about rescuing the economy from the disaster. Chairman Martin said that he believed that there was every expectation that the economy was facing a roaring fourth quarter which would include a record Christmas shopping season as well as the forces we have been talking about. He did not think that a somewhat tighter credit policy would keep the fourth quarter of this year from being an extremely good one.

Turning to the question of policy to be followed, Chairman Martin said that the consensus seemed to be fairly clear. It appeared that no one wished to disturb the Treasury's financing and that the

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Committee should keep as even a keel as it could until that was completed, recognizing that it was difficult to maintain an even keel. The projections furnished the Committee included an allowance for normal growth, Chairman Martin noted, and he gathered that it was the intention of all present this morning that the System take care of normal growth and reasonable credit needs of the economy. However, it did not wish to have credit flow to people who should have gone to the long-term capital market for funds but who did not go there because they felt that the Federal Reserve would not have a tighter money policy during the fall of this year when the election was coming up. The System would be compounding the disaster if markets are misjudged as the automobile industry misjudged the market early this year. The Chairman said that he agreed with the comment Mr. Irons had made that an increase in discount rates generally to the 3 per cent level would not be a dramatic move and that, in fact, banks would be surprised if that action were not taken. He added the comment that, in his view, the "stalking horses" to which Mr. Powell had referred in speaking of the Reserve Banks now having a 3 per cent discount rate have done a real service. Further commenting on credit policy, Chairman Martin said that he believed the consensus of this meeting to be that, during the period up through payment for the current Treasury offering, the Committee should try to keep as even a keel as possible and thereafter tend to resolve doubts on the side of tightness, gradually moving negative free reserves

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upward.

In response to a question from Mr. Vardaman, the Chairman stated that he deliberately left out of his comments any maximum figure to which negative free reserves might be permitted to go.

Mr. Rouse stated, in response to Chairman Martin's request for his comments, that the foregoing was his understanding of the consensus at this meeting with respect to the policy to be pursued between now and the next meeting of the Committee.

Chairman Martin then turned to the directive and suggested that the elimination of the part of clause (b) to which Mr. Hayes had referred would be desirable. While the suggestion Mr. Vardaman had made could be taken, he felt the preferable procedure would be simply to delete from the current directive the instruction that the Agent Bank take into consideration deflationary forces in the economy. With this change, clause (b) would read, "to restraining inflationary developments in the interest of sustainable economic growth,..."

Mr. Vardaman said that he would concur in this procedure, and Mr. Rouse stated that he had no suggestions for change in the dollar limitations in the directive.

Thereupon, upon motion duly made and seconded, the Committee voted unanimously to direct the Federal Reserve Bank of New York until otherwise directed by the Committee:

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(1) To make such purchases, sales, or exchanges (including replacement of maturing securities, and allowing maturities to run off without replacement) for the System open market account in the open market or, in the case of maturing securities, by direct exchange with the Treasury, as may be necessary in the light of current and prospective economic conditions and the general credit situation of the country, with a view (a) to relating the supply of funds in the market to the needs of commerce and business, (b) to restraining inflationary developments in the interest of sustainable economic growth, and (c) to the practical administration of the account; provided that the aggregate amount of securities held in the System account (including commitments for the purchase or sale of securities for the account) at the close of this date, other than special short-term certificates of indebtedness purchased from time to time for the temporary accommodation of the Treasury, shall not be increased or decreased by more than \$1 billion;

(2) To purchase direct 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 total amount of such certificates held at any one time by the Federal Reserve Banks shall not exceed in the aggregate \$500 million;

(3) To sell direct to the Treasury from the System account for gold certificates such amounts of Treasury securities maturing within one year as may be necessary from time to time for the accommodation of the Treasury; provided that the total amount of such securities so sold shall not exceed in the aggregate \$500 million face amount, and such sales shall be made as nearly as may be practicable at the prices currently quoted in the open market.

Chairman Martin referred to the proposal that Mr. Sproul had made in his memorandum of May 3, 1956 that the Committee authorize the Account Management to make offsetting purchases and sales of Treasury bills for the purpose of altering the maturity distribution of the System open market account when, in the Manager's judgment, such purchases and sales

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would not distort the functioning of the market and would improve the capacity of the account to perform effectively in supplying or absorbing reserves. A memorandum from Mr. Robertson relating to this proposal had been distributed to the members of the Committee under date of May 21, 1956 and an additional memorandum prepared at the Federal Reserve Bank of New York had been distributed under date of June 4, 1956. Chairman Martin went on to say that he did not think that any of the members of the Committee felt that this was a matter of earth-shaking importance but that even in terms of the present limited proposal for swaps in Treasury bills, there was some merit to using this means sparingly. He then called upon Mr. Robertson who had indicated doubts about the desirability of the proposal.

Mr. Robertson said that he would reiterate the statement of Chairman Martin that the proposal was not of great importance one way or the other. In addition to the material presented in the various memoranda, he stated that he would be glad to have Mr. Hayes' views regarding the proposal and that if he (Mr. Hayes) had not had an opportunity to study it, it did not seem of pressing importance that it be discussed at this meeting. In addition, Mr. Robertson said that he would suggest that before acting on the proposal, the New York Bank ascertain the views of dealers as to the extent of swaps and their attitude toward having the System account engage in such transactions.

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Mr. Hayes said that he had had an opportunity to study the memoranda referred to and had discussed them with Messrs. Treiber and Rouse. While he and Messrs. Treiber and Rouse did not feel that the matter was of vital importance, he was ready to discuss the proposal and act upon it this morning. Mr. Hayes went on to say that he felt Mr. Robertson's suggestion as to having the views of dealers was desirable, that it was his understanding that Mr. Rouse had made some effort to find out their attitude, and that he thought the matter might be disposed of at this time as well as later. Mr. Hayes then called upon Mr. Treiber for comment.

Mr. Treiber said that the proposal before the Committee was that the management of the System account be authorized to make swaps in Treasury bills when such purchases and sales (1) would improve the capacity of the account to perform effectively in supplying or absorbing reserves and (2) would not distort the functioning of the market. System holdings of Treasury bills are relatively small, Mr. Treiber said, and when the System has few or no bills of a particular issue, difficulties may be presented. First, when the System has occasion to sell bills to absorb reserves it might not have the issues for which there is demand in the market, and there may be less demand in the market for the issues it does hold. The second difficulty involves run-offs. Allowing Treasury

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bills to run off is generally simpler and less disturbing to the market than selling an equal quantity of Treasury bills in the market. Mr. Treiber noted that it is customary for the System to let Treasury bills run off in January and for that reason it is desirable to hold some bills maturing in January. He felt that it would be desirable for the System account to get into a position where it would have bills that it could permit to run off at that time, or where it would have bills that could be rolled over into January bills. He also stated that the proposal contemplated that swaps would be made only occasionally and would usually be undertaken in response to the initiative of the market. They would, as stated before, be made only when that would not disturb the functioning of the market.

In response to a question from Mr. Shepardson as to what he meant by the statement that swaps would be made in response to the initiative of the market, Mr. Treiber said that usually dealers will have orders for various issues of bills and if they are unable to fill those orders out of their own supply, they initiate discussions with other dealers in the market or with institutional investors such as insurance companies to find out whether they can work out a trade to get the securities needed to fill the order. Such inquiries come to the attention of the trading desk frequently, Mr. Treiber said, and that was the point he had in mind in stating that the trades would be made at the initiative of the dealers.

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Mr. Rouse noted that this was one basis for the statement that it was believed that dealers would not object to the making of swaps by the System account. However, he added the comment that he felt if the authority were given, the account management should feel free to make such swaps within the limits of the proposal in the memorandum, whether a dealer initiated the transaction or not. Mr. Rouse also said that he would be very happy to check with dealers along the lines suggested and that he thought it might be desirable to make such a check.

Mr. Robertson suggested that in discussing the proposal with dealers it might be desirable also to find out their attitude toward the Reserve Bank initiating such swaps rather than participating in them only when initiated by a dealer.

Chairman Martin stated that the suggestion for checking these points with dealers might be followed. However, he wished to make clear his personal position. In principle, he said that he felt that swaps for the System account were wrong. He did not believe in being hide-bound, however. Nevertheless, even if the proposal was limited to making swaps with interest bearing money, which was what Treasury bills are, the question was only a matter of degree. Every time the System account tended to depart from what he called the "free market" principle, it was taking a step in the wrong direction and it was likely to find that others would be pressing it to move a step further.

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Chairman Martin said that he never felt hesitant about stating the free-market principle but that he would not wish to take a narrow view of this proposal and that, subject to checking the attitude of dealers along the lines suggested, he would be disposed to go along with the limited authorization suggested even though he felt it to be a step in the wrong direction.

The discussion of this topic concluded with the understanding that the New York Bank would attempt to obtain the views of dealers as suggested, after which the matter would be placed on the agenda for further discussion.

Chairman Martin suggested that it might be desirable to hold the next meeting of the Committee on Tuesday, August 21, two weeks hence, with the thought that the following meeting would be on Tuesday, September 11. There was some discussion of possible dates for meetings, at the conclusion of which it was agreed that the next meeting of the Committee would be held on Tuesday, August 21, 1956. During the discussion, it was also suggested and understood that tentative dates for subsequent meetings would be set for Tuesday, September 11, and Tuesday, September 25, 1956.

Mr. Robertson said that this was an appropriate time for the members of the Board of Governors to express their appreciation to the Presidents of the Federal Reserve Banks for their cooperation during Operation Alert 1956 in the period July 20-25, 1956, inclusive. He noted that comments and suggestions had been submitted by the Presidents,

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that they were now being reviewed, and that it was contemplated that there would be a discussion of this subject at the next meeting of the Presidents' Conference, tentatively suggested by Mr. Leedy during the week that would include the meeting of the Open Market Committee on September 25, 1956.

Mr. Johns noted that Mr. Mangels had referred to a check he had had made by his Bank's Research Division as to the effect of a reduction in reserve requirements and an increase in the deferred availability schedule of the Reserve Bank. He went on to say that Mr. Rouse had also suggested at the meeting of the Committee on July 17, 1956, that the System give more consideration to the influences of float on credit and on the conduct of open market operations. Mr. Johns stated that, while various studies of the subject of float had been made by the System in the past, they had always been directed primarily in terms of operating problems in handling checks for collection. It was his thought that it would be desirable for the Federal Open Market Committee to make a study of the subject because of the effect of fluctuations in float on open market operations.

After some discussion as to whether such a study should be by a committee reporting to the Federal Open Market Committee or whether it would be preferable to have it made by a committee reporting to the Conference of Presidents of the Federal Reserve Banks, it

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was agreed unanimously that Chairman Martin in consultation with Mr. Leedy, as Chairman of the Presidents' Conference, be authorized to appoint a committee along the lines suggested by Mr. Johns.

Secretary's note: Following the meeting, the Secretary was informed by Chairman Martin that, after consultation with Mr. Leedy, he had appointed Messrs. Robertson, Johns, and Erickson as members of a Committee on Float, with Mr. Robertson to serve as chairman of the committee and with the understanding that the results of the study to be made by the committee would be reported to the Federal Open Market Committee.

Thereupon the meeting adjourned.


Secretary