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 Monday, February 18, 1957, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Hayes, Vice Chairman
Mr. Balderston
Mr. Erickson
Mr. Fulton
Mr. Johns
Mr. Mills
Mr. Powell
Mr. Robertson
Mr. Shepardson
Mr. Szymczak
Mr. Vardaman

Messrs. Allen, Bryan, Leedy, and Williams, Alternate Members of the Federal Open Market Committee

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

Mr. Riefler, Secretary
Mr. Thurston, Assistant Secretary
Mr. Thomas, Economist
Messrs. Abbott, Hostetler, 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

Messrs. Bopp, Daane, Mitchell, and Tow, Vice Presidents, Federal Reserve Banks of Philadelphia, Richmond, Chicago, and Kansas City, respectively; and Mr. Atkinson, Economist, Federal Reserve Bank of Atlanta

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the Federal Open Market Committee held on January 28, 1957, were approved.

Before this meeting there had been distributed to the members of the Committee a report prepared at the Federal Reserve Bank of New York covering open market operations during the period January 28 through February 11, 1957, as well as a supplementary report covering commitments executed February 13 through February 15, 1957. Copies of both reports have been placed in the files of the Committee.

Mr. Rouse noted that the report of open market operations during the past three weeks was longer than usual, partly because of his belief that the Committee would be interested in a detailed description of the System account sales of certificates of indebtedness and Treasury notes and the market's response to these sales. Sales of certificates and notes had not commenced until Friday, February 8, when System holdings of bills declined below $250 million, Mr. Rouse said, adding that as of Friday, February 15, System bill holdings were down to $178.3 million.

Mr. Mills inquired whether as a matter of policy it would be desirable in the future to make an immediate and complete explanation of the purpose of a departure from an established practice where the transactions involved represented a change in technique and not a change in policy (in this case, departure from the practice of limiting transactions for the System account to Treasury bills) as a means of making certain that the market was fully informed.

Mr. Rouse said that the transactions in certificates and notes had been handled in a manner (which he described) intended to make certain that dealers would know that the transactions were for the System account. Although he felt certain that there had been very little misunderstanding, he agreed that, looking backward, there would have been no harm in indicating even more clearly what was being done.

Mr. Robertson said that he had the same feeling as Mr. Mills: the System might benefit by making even plainer in the future any changes of this character. He suggested the possibility of utilizing the morning conference with dealers as a means of spelling out such changes so as to avoid any possible confusion. He then inquired whether Mr. Rouse felt that, in hindsight, it was appropriate to sell certificates and notes at a time when the System account still held almost $250 million in Treasury bills.

Mr. Rouse responded that at the time he had felt such sales were appropriate and desirable, and it still seemed to him that was the case. He reiterated that since February 8 sales of bills had brought holdings down to $178 million.

Mr. Hayes suggested that whether the figure was $200 million or some other figure, it was clear that there was some level of System holdings of bills below which the System would ordinarily not wish to go in order to maintain a supply of bills in the event it became desirable to withdraw a relatively large amount of reserves from the market very rapidly. He said that he had accepted Mr. Rouse's judgment on the point under discussion.

Mr. Erickson inquired whether, if it announced a change in procedure of this type, the Committee might set a precedent which would make it necessary to explain every future change in operating procedure.

Mr. Rouse stated that there might be some such feeling, although he did not think it would be necessary to make explanations of all changes of this type.

> After some further discussion, upon motion duly made and seconded, and by unanimous vote, the open market transactions during the period January 28 through February 15, 1957, were approved, ratified, and confirmed.

Mr. Young's statement on the economic situation, made at Chairman Martin's request and as a supplement to the staff memorandum distributed under date of February 15, 1957, was as follows:

> Towards the end of 1956, business and financial observers were in unusual agreement that further advances in business activity and further creeping inflation were to be expected for the year 1957. Subsequent reappraisal has given rise to doubts. Indeed, views in the direction of a topping-out of the inflationary advance have come to be expressed more frequently, with the implication that a phase of downward deflationary adjustment may be predestined for later in the year. It seems appropriate at this meeting to inventory briefly these elements that the doubters are pointing to as casting their shadows before.
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> Industrial production has hesitated in January and slipped back one index point. Of the 24 major industrial groups entering into the make-up of the index, some 14 have shown declines in output since October of last year and 3 no change in output. Absence of strength of indications of weakness were especially characteristic of consumer goods industries. Gains in industrial consumption of coal and electric power over a year ago have been narrowing, and freight car loadings have been moderately under year-ago levels.

While the general level of commodity prices at wholesale has continued to rise--rising 1/2 per cent from mid-December to mid-January and probably further to mid-February--the advance in industrial commodity prices has slackened since late autumn and, among commodity groups, the frequency of price advance has been reduced. Prices of a number of industrial materials and scrap, furthermore, have been declining, and since early December average prices of basic commodities have receded 4 per cent to about the level obtaining prior to the closing of the Suez Canal. Caution in forward buying has come to be a feature of basic material and scrap markets, of markets for some steel and metal products such as copper, and of markets for textiles and for paper.

For some months now, industrial construction has been below a year ago and, since last spring, residential contract awards in millions of square feet have been falling. Nonresidential construction awards for business purposes have also been declining, with contract awards dropping from spring through the year end. Available evidence, moreover, suggests that plant and equipment expenditures by manufacturing industries are in the process of leveling off; some observers would say already declining, because for several months, some indexes of machinery orders have been showing downdrift. Unfilled orders in durable goods industries have been little changed since August in contrast to the earlier situation of a mounting order backlog.

While employment over-all has held up well in recent months, it can be argued that some weakening in manufacturing employment has recently occurred. Since October, small, steady, month-to-month declines in durable goods employment have been evident and declines have also been registered over this period in employment in some nondurable goods lines. The number of industries represented in the declines has been growing. Manhours worked per week have also declined in about half of the major industry groups since October, with other industries mainly stable. In January there was a general decline in manhours worked in durable goods industries and also a decline in some major nondurable industries.

Business inventories have risen through 1956 at about the same rate as in 1955. The increase in manufacturing inventories has been more than sales, so that inventory-sales ratios in manufacturing are higher than a year ago. With substantially increased capacity to produce and to distribute finished product than two years ago, total business inventories of $88.5 billion and $6 billion higher than a year earlier may well be on the high side.

Corporate internal funds have been lower in relation to their plant and equipment expenditures in 1956, resulting in heavier reliance on external sources of funds and lowered corporate liquidity. While the fourth quarter bulge in business sales and profits relieved corporate financial pressure and facilitated the pay-off of bank loans in January, many recent annual reports of corporations indicate that 1956 was a year of reduction in corporate financial fat.

In Western Europe, industrial production has been relatively level now for the past three quarters, and for several weeks the drift in world commodity markets has been downward, with some raw material prices declining well below pre-Suez levels.

The foregoing inventory of slackening momentum elements is clearly impressive enough to occasion caution and to prompt some bears to come out of hibernation to test feeding grounds. It is not yet impressive enough, however, to justify a firm conclusion that rolling adjustment at rising levels of total activity, and with inflationary pressures, is close to an end and that general deflationary adjustment is now a greater prospective likelihood. Before any such conclusion is reached the inventory of elements to be weighed needs to be extended. For instance:

Industrial production, while not rising, continues at about record levels. Small declines in some industries have about been offset by gains in others. Important types of steel remain in short supply and are a limiting factor in further expansion of some lines of output. Declines in durable goods output, especially in output of machinery, reflect reduced production of mechanical parts for consumer durable goods. Unfilled orders for durable goods industries, while not rising since August, remain about an eighth larger than a year ago, and are particularly heavy in producer's equipment and machinery lines.

In December, work on architects' drafting boards other than factory buildings, after declining gradually for several months, rose sharply. In January, contract awards for construction of manufacturing and commercial facilities were also up sharply. Awards for industrial building were up more than half of the average for the fourth quarter and commercial contract awards were up about a third. Capital expenditure appropriations of large corporations, after a marked reduction in the third quarter, are reported to have shown an appreciable reversal in the fourth quarter.

While residential construction activity is down, recent month-to-month declines in starts and awards have been smaller than earlier, and careful review of reports on the housing market indicates considerable strength, and not weakness. Prices of old and new houses are reported to be firm; vacancies are low; vacant houses for sale have been declining; rents on rental housing are still rising; a large volume of home sales transactions continue to find financing; and the current rate of mortgage lending is high by any standard, except 1955. Mortgage commitment funds continue tight and market demand for Government underwritten mortgages is slack.

Altogether the labor market is still strong and not weak. Nonfarm employment is at a record level; demands for nonmanufacturing employees continue active, after allowing for seasonal factors; no large lay-offs of manufacturing employees have been reported; and total employment, seasonally adjusted, is still low--about the same as a year ago and the average for 1956.

Government spending for goods and services--Federal and State and local government combined--has been rising steadily and further steady rise seems to be in prospect.

Consumer incomes have risen further this year and consumer spending at retail in January was about the record level of December--5 per cent ahead of last year. In contrast to 1955, consumers in 1956 increased their holdings of financial assets more than their total debt, thus strengthening their aggregate financial position. New automobile sales in January and the first part of February have been on the strong side, all things considered, even if below some highly optimistic expectations. Used car sales have been especially strong and used car prices, after allowance for depreciation, continue stable.

Business financial pressures seem to have eased some early this year; the upward trend in business failure liabilities appears to have leveled off; market reception to new corporate issues has been generally favorable; and business optimism, as reflected in the latest Dun and Bradstreet survey of sales and profits expectations, taken in early January, ran higher than was shown by the preceding survey, taken in the third quarter of 1956, and the increase in optimistic expectations was shared by most manufacturing and retail groups. Demands for long-term business funds continue very strong.

As to agriculture, income of farm proprietors holds at about year-ago levels, and farm prices recently have been fairly stable at about 5 per cent above last year.

In Western Europe, productive resources have been intensively utilized all through the past year, so that further gains could be registered slowly. The fact that the post-Suez fuel shortage had little visible impact on total industrial production through December is at least suggestive of underlying strength, especially in the face of declines in raw materials prices. Indeed, these declines in some cases reflect more ample supply conditions from expanded output rather than any appreciable curtailment of demands. Recent downward adjustments of discount rates in Britain and Germany seem to be special adaptations to domestic financial problems rather than early indications of a general economic and credit easing in Western Europe.

> We may conclude this point and counterpoint inventory of the current economic situation in this way. There is evidence of some slackening in the momentum of inflationary advance, but there is as yet no clear-cut evidence of a conjuncture of forces that would indicate a halting of the advance in the foreseeable future with a greater than even possibility that downward deflationary correction will follow. If or as such evidence develops in ensuing weeks, your staff will place it before you promptly. The financial problem of the economy, in my judgment, continues to be that of demands in the aggregate pressing against aggregate resource supply. Basically, the situation is still inflationary, though with moderate abatement of inflationary tendencies.

Mr. Vardaman said that he happened to be one of those who felt that the rise in economic activity had topped off. He inquired of Mr. Young as to what clear-cut evidences of a downward trend in economic developments would have to appear before the staff indicated to the Committee that a downward trend was developing.

Mr. Young responded that one of the points that had been emphasized particularly by those who felt that we may have topped out was that business expenditures for plant and equipment were leveling off and even declining. There has been a supercolossal rise in such expenditures, he said, and at some point it was inevitable that they would top out and turn down. Although such a topping out appeared to be taking place in that particular field, Mr. Young said that this did not mean that a downward turn in the economy generally was developing, particularly since demands for additional plant facilities even now were at an extremely high level and still rising. Outside the capital expenditures field, a number of indicators continued to show great strength and advance, Mr. Young said, noting that plans on architects' drafting boards and construction awards during January had risen sharply. The economy was at a point of very intensive utilization of resources and if plans for expansion were to continue to rise, the problem presented would be even more difficult. Mr. Young concluded by saying between this and the next meeting evidences might appear to indicate a general topping off in the economy and, if so, these would be brought to the attention of the Committee at once.

Chairman Martin next called on Mr. Thomas for a statement on the credit situation.

In opening his remarks, Mr. Thomas stated that last week he attended a conference of business economists in Washington at which the consensus was that business expenditures were high and not declining, although there was some indication that they might be leveling off. A careful analysis of the situation indicated that business capital expenditures would continue at a high level through 1957 on the basis of business already booked.

Mr. Thomas then made a statement on recent financial developments as follows:

> Credit developments in recent weeks continue to indicate a relaxation of pressures. The rate of bank loan liquidation has been well-nigh unprecedented; bank reserve positions have been less strained, despite heavy absorption by System open market operations; money rates have declined sharply; and the tone of the bond market has changed so much as to permit the sale of a very large volume of new issues of securities at declining yields, while the stock market has been weak.

This easing, however, does not lead to a conclusion that a general downturn in economic activity has begun or is imminent. Some relaxation is customary for this time of the year. While the readjustment in money rates, for example, has been somewhat sharper this year than usual, it followed a more precipitous rise, that was probably overdone. Bond yields, particularly on corporate issues, are still high by any previous postwar standards. Stock prices, while near or below the lows of 1956, are still not far below the highs of 1955. Bank loans outstanding are larger than they were a year ago and two years ago by amounts of growth that could not be indefinitely sustainable. The large volume of new corporate issues provides a basis for continued heavy investment expenditures by businesses and by State and local governments.

Federal Government expenditures have been increasing and its excess outlays, for various reasons, have been larger and have extended longer than is usual at this season. In fact, the reduction in Treasury cash balances has been a most important factor in the easing of the money markets.

Although there are indications of a lower level of housing construction and financing and the prospects for automobile sales are still uncertain, consumer spending has generally continued at a high and rising level. The mixed movements of commodity prices indicate a moderating of upward pressures but no general downturn. Wage increases continue to create cost-profit squeezes.

At the best, current developments may be considered as the relaxation of inflationary pressures which has been desired and toward which monetary policies have been directed. Whether this is but a temporary lull in the inflationary pressures, or the beginning of a downturn, small or large, or the attainment of high-level stability only time can tell. There are no strong indications that either of the first two possibilities is more likely than the last more desirable course of events.

Treasury difficulty in building up a cash balance to a more workable level has been due to a combination of factors. Payments, particularly for defense purposes, have been larger than were expected; redemptions of savings bonds have continued rather large; and receipts have fallen somewhat short of estimates. To what extent the short-fall in receipts is an unexplained lag in tax payments or a lower level of tax liabilities than expected cannot yet be determined. It seems evident that the Treasury will need new financing of perhaps $3 billion in the next two months. One of the decisions to be made is whether to continue to raise $200 million a week through additional sales of bills or whether to make a special cash offering and curtail the new weekly borrowing.

Corporate security issues for new capital in February promise to be close to the near record January volume, and schedules indicate no let-up in March. While there is a feeling that business expenditures for plant and equipment may be leveling off, available evidence indicates that they are likely to continue at a high level through this year. Business borrowing demands are expected to remain large. Flotations of State and local government securities will evidently be larger than were expected earlier. Growing acquiescence by issuers in the higher level of rates, together with the large volume of public works expenditures being planned, indicates continued absorption by this sector of any funds that may be available.

Bond yields, both on new and on outstanding issues, have declined in recent weeks, but the decrease in corporate yields has been moderate, compared both with the previous rise and with the declines in governmental issues. Yields on outstanding high-grade corporate bonds are still higher than at any time before November, while those on Treasury bonds are close to the levels of last August. State and local government issues, which showed a more precipitate rise in yields, are in an intermediate position with respect to the decline. Last fall's rise in yields on medium-term Treasury bonds to well above those on long-term bonds has been largely eliminated, and the yield structure is again comparatively flat. Both the strength in bond prices and the weaknesses in stock prices can be explained by the relation between yields on stocks and bonds, together with the apparent leveling out of corporate profits. Investors are evidently shifting from stocks to bonds.

Treasury bill yields, while fluctuating considerably, are at a higher level relative to bond yields than was the case prior to November. Although banks and dealers have initially absorbed a large portion of recent new bill issues, there has been a strong secondary market from nonbank buyers. These demands reflect in part reinvestment of funds obtained from maturing Treasury issues, in part temporary investment of the proceeds of new security issues, and perhaps in part some cash flow to corporation.

Reasons for the probably unprecedented liquidation of bank loans since the beginning of this year are as yet difficult to determine. Much of the reduction is seasonal--as in food, liquor, and tobacco manufacturing, trade lines, commodity dealers, sales finance companies, and construction--and in some cases reflects a reaction from more than seasonal increases that preceded. The preceding temporary needs were either larger than usual or were overestimated. Some of the decline in loans may have been made possible by the new capital issues, but little of it can be related directly to this source. Perhaps more will come as the proceeds of recent new issues become available. Indirect evidence indicates that the decline in loans occurred entirely at banks in leading cities.

The decline in bank investments has been less than in the same period last year, reflecting substantially smaller reductions in securities other than Treasury bills. This may be an indication of the lowered liquidity position of banks and the lower level of bond prices, as well as of the larger decline in loans.

Much of the decrease in bank credit this year has been counterbalanced by larger declines than a year ago in U. S. Government and interbank deposits. The decrease in demand deposits adjusted at banks in leading cities in the past six weeks has been smaller than in the same period last year. Time deposits have increased compared with a decrease last year. The decline in demand deposits has been close to the usual seasonal amount. Following a large increase in December, the return flow of currency in January was exceptionally large and exceeded seasonal expectations by over $400 million. It appears that the total money supply showed a greater than seasonal decline in January.

Member bank reserve needs in recent weeks have declined more than usual for this period, owing largely to the sharp decline in money in circulation and to a somewhat larger than expected drop in required reserves. The latter was due principally to the low level reached by Treasury tax and loan accounts. The increase in the gold stock, resulting from the IMF sale of $300 million of gold to the U. S. Treasury, also added to reserve availabilities. Movements of float, though at a high level, have conformed fairly closely to the seasonal pattern.

The increased availability of reserves has been fully offset, with some lag, by reduction in the System Open Market Account. This decline by the end of this statement week will have amounted to nearly $2 billion since the last week of December. Consequently net borrowed reserves have returned to around the quarter billion dollar level for the first time since early October, after showing a net free reserve position during most of January.

In the current statement week, as shown in the table of projections, a further decline in Treasury balances at the Reserve Banks below the recent low level and the usual mid-month high level of float are expected to provide an abundance of reserves, notwithstanding a continued substantial reduction in System holdings. Next week, however, this situation should change sharply and, in the absence of System purchases to supply reserves, net borrowed reserves might rise to around $400 million. In the following two weeks they might be in the neighborhood of $500 million. Any System purchases to moderate this increase should probably be offset by sales in some subsequent weeks, particularly when float rises. Hence repurchase contracts would be an appropriate medium for covering some of these variations.

From the standpoint of policy objectives, the question is how much restraint in credit should be applied in the existing and prospective situations. Evidently any more stringent restraints at this time would be unnecessary and inappropriate. On the other hand, no occasion for relaxation is evident. In view of the changed attitude of banks, net borrowed reserves might be kept around $250 million, or about half the level prevailing in March and April last year. If, however, there is a pronounced reversal in the trend of credit demands with a sharp increase in bank loans, borrowings should be permitted or made to increase above that level. On the other hand, if credit liquidation continues beyond the usual seasonal pace, a somewhat lower level of reserve needs would develop and member bank borrowings might be permitted to decline.

The final answer lies, as always, in the course of production and prices, credit demands and interest rates, rather than in the level of member bank borrowings. The forces for rises in costs and prices are apparently still in operation.

Chairman Martin said that as a prelude to the discussion of the situation this morning, he wished to report that he had talked with Secretary of the Treasury Humphrey and Under Secretary Burgess during the past few days. He had assured both the Secretary and the Under Secretary that he would see to it that the Open Market Committee was informed as to the problem the Treasury was facing, and he said that he felt Mr. Thomas had pointed up the problem of the Treasury's cash position very well. The Secretary was concerned about the Treasury's balance, Chairman Martin said, noting the attrition that had taken place on the Treasury's latest issue. Mr. Burgess wanted the Committee to know that the Treasury might have to come to the Federal Reserve for direct borrowing, since it did not know whether it would be feasible to go to the market for funds in an amount such as Mr. Thomas had suggested might be needed during the next two months. The Treasury was also at a crossroad on the savings bond program and some time might elapse before it knew how the program would work out.

The Chairman then called upon Mr. Hayes, who made a statement with respect to economic activity and open market policy as follows:

> 1. We continue to find evidence that the country's economic activity as a whole may be flattening out--admittedly at a high level, but with nothing in sight to provide upward momentum on the scale witnessed last fall. At the same time there was no clear evidence of serious weakness in the economy.
> 2. There are some fragmentary signs that inventories may no longer be growing as rapidly as in 1956, and there is further confirmation of a leveling out of capital expenditures. For example, machinery orders and industrial construction contracts in December were appreciably lower than a year earlier. Some industries are reported to have decided to stretch out their plant expansion programs.
> 3. The outlook in the automobile, steel, and residential construction industries remains substantially as it was at the time of our last meeting. In our view it is still too early to say whether automobile sales for 1957 will come up to early expectations of a gain of perhaps 10% over 1956. Housing starts will probably be lower than last year, and lower steel operating rates in relation to capacity are expected soon.
> 4. Divergent price tendencies for finished goods and sensitive scrap and waste materials have now continued for a good many weeks. It would be unusual for this condition to persist for an extended period, and it is at least possible that the weakness in scrap prices portends a more

general easing in demand-supply relationships which may ultimately be reflected in lower prices for finished goods.
5. The most recent figures on bank loans at all weekly reporting member banks showed a continuation of the pronounced January decline, although the pace of the decline had slackened, and the February 13 data show an increase in business loans at the central reserve city banks. The decline in the first six weeks of this year was the largest in recent years. To a considerable extent this is doubtless merely a reversal of the sharp seasonal upswing of November and December, but the size of the drop suggests that it has gone beyond this point. Bankers seem to look for somewhat less of a bulge in borrowing for March taxes than had previously been expected. The trend toward sharply lower corporate liquidity which was so prominent a feature of last year's financial developments appears to have slowed or even to have been reversed, temporarily at least--due doubtless in part to the recent heavy volume of successful corporate capital flotations, and perhaps also due to the temporary sharp drop in Treasury balances, as well as a possible shrinkage in inventories.
6. While the Treasury's first major refunding problem of the year is now out of the way, we must reckon with substantially larger Treasury cash needs than were looked for at the beginning of the year or even at our last meeting. The Treasury's present cash problem, together with the facts that dealers still hold sizable positions in the securities offered in the refunding, and that our holdings of bills are now minimal, have created some difficulty in maintaining net borrowed reserves in the current week. We are not unduly concerned over this development, however, since the market will doubtless recognize this situation as a reflection of temporary influences, notably the difficulty with Treasury's balance and the bulge in float.
7. We feel that this is clearly a time when we should make no overt change, in either direction, from the policy of restraint which we have been following. However, if some moderate easing of the banks' reserve position should be caused by further declines in total bank loans and investments, we question whether the System should counteract it. We can see no reason to consider a change in the discount rate under present conditions.
8. While there is no longer the degree of unsettlement in the financial markets that prevailed some weeks ago, there are some continued uncertainties and irregularities in the capital markets and continued unsettlement in the international

situation. There is some question in my mind as to whether the directive might appropriately be modified at this time. Perhaps it would be well to defer discussing this point till we have heard the views of the others present as to general policy.

Mr. Johns said that he found no reason to disagree with the views expressed by Mr. Young in appraising the current situation. After reviewing the situation with his staff last Friday, he failed to see any convincing evidence that what was going on amounted to a beginning of recession. He was rather inclined to like what he saw; perhaps there was some leveling off of the boom and of inflationary pressures, and, if so, this was all to the good and what the System had been striving for for many months. Rather than deflation, he was inclined to feel that current developments indicated a somewhat better allocation of resources, and he liked this development. Aside from this, Mr. Johns said that there were some forces that might produce a resurgence of inflation and he felt the Committee should keep on guard against these. Therefore, his view was that there should be no overt change of policy at this time. He would favor maintaining about the same degree of restraint that had been the Committee's target for the last two meetings. He would favor no change in discount rate at this time, would like to see net borrowed reserves somewhere in the neighborhood of $200-250 million, and since he did not like to tinker with the Committee's directive any oftener than necessary, he would prefer not to amend the directive at this meeting.

Mr. Bryan said that there was nothing in the Sixth District that would warrant a detailed report to the Committee this morning. The tendencies, as in the national picture, were somewhat more mixed than they had been previously but generally speaking he could deduce no convincing signs that the momentum of expansion had shifted. On the national picture, Mr. Bryan said that he saw no reason to differ from the conclusions expressed thus far this morning. The picture was more mixed than it had been, but it did not seem clearly to portray an ebbing of the tide at present. A difference in emphasis that he would make was his belief that the Committee's policy had not been recently one of restraint but one of rather definite ease. This may have been the correct policy but in any event it was now time for the Committee to abandon at least for the moment all talk of getting back to the tightness of last November and early December. There was some danger that we could get an even greater ease than we have had, Mr. Bryan said. The bill rate could go temporarily well below the discount rate and this would be a blunder in his opinion. He felt the System should make constantly such sales into the market as to try to keep the bill rate somewhat above the discount rate. He would like to have a greater posture of restraint than the Committee has had recently.

In response to Chairman Martin's question as to whether he felt the recent ease had been "overt" or whether it had been "inadvertent," Mr. Bryan said that the ease to which he referred had arisen to some extent out of the free reserve concept. He would commend the desk in having gotten net borrowed reserves between the $200-300 million mark, which had been suggested as a desirable objective at the preceding meeting. In his opinion, Mr. Bryan said, the recent ease had been inadvertent ease.

Mr. Williams stated that in preparation for this meeting representatives of the Philadelphia Bank had talked with a number of economists for industrial concerns in the Third District during the past few days, and he reported the results of these discussions, particularly whether the industrial firms had modified their plans for capital expenditures during 1957. A number of the concerns interviewed were smaller ones while some of them were large national organizations. The substance of Mr. Williams' report was that in most cases the companies had made no move to cut back or postpone their capital expenditure programs but were planning to go ahead with projects that had been announced. In some cases, firms reported that orders had fallen off early this year, but in a number of cases the most recent data indicated a resumption of orders. In general, the inventory situation was not causing concern. However, Mr. Williams noted that the prospects for 1957 were not now being viewed with as much exuberance as they had been at the turn of the year, representing a more conservative appraisal of business prospects. This seemed to reflect primarily a shift in psychology rather than any fundamental weakening in the business and financial situation. Mr. Williams suggested that perhaps as far as capital expenditures were concerned, the evidence he had presented indicated that there might be a distinction between large and small corporations and that some of the announcements of postponement of plans that had appeared in the press received undue attention because they came from large firms.

Continuing, Mr. Williams reported that demand for bank loans in the Philadelphia District continued strong, with some easing having appeared within the past few weeks. Various other indicators of economic activity continued generally strong, although Mr. Williams noted that new automobile registrations in January of this year were 13 per cent below January a year ago. Summing up, Mr. Williams said that the outlook seemed to run counter to the psychology as indicated by press reports. His attitude was that the Federal Reserve should make no significant change in policy at this time.

Mr. Fulton said that businessmen in the Cleveland District were optimistic. They talked caution but were going right ahead with their plans. Operations of the steel industry seemed satisfactory to management, he said, and one member of the industry had commented that the newspapers were doing the worrying for the steel companies. Takings of automobile steel had been about as expected in recent weeks, but some letdown in appliance takings had been noted. Demand for construction steel continued good. Industry was going ahead with plans for construction, and the higher cost of credit was not deterring such programs. Some bankers expected a fairly substantial rise in tax borrowings during

March because of the reduced liquidity position of corporations. Consumers were calling more frequently for terms of 36 months in purchasing automobiles than had been the case earlier.

Mr. Fulton said that he believed no change should be made in the Committee's present policy and that net borrowed reserves should be held about the $250 million level. During March, banks should be permitted to come to the discount window to take care of their needs in meeting the prospective rise in loan demand. He referred to clause (b) of the Committee's directive, stating that he felt the unsettled conditions in the money and capital markets that the Committee had in mind when it added the second part of the clause had changed, and he suggested that this part of the directive might be modified so that it would indicate that transactions should be with a view "to restraining inflationary developments in the interest of sustainable economic growth, while recognizing that activity in some segments of the economy has receded from peak levels." Mr. Fulton said that he would not change the discount rate at this time.

Mr. Shepardson said that he felt Mr. Young had done an exceptionally good job in pointing up the divergent trends in the economy. While there were some indications of leveling off, he felt these were all to the good and were in the direction toward which the Committee had been working. There were still very strong inflationary pressures that the Committee should bear in mind and this was no time to make any change toward slackening off restraint on credit expansion. Mr. Shepardson said that he had felt restraint had not been quite up to the mark that the Committee had in mind for the last few weeks, and he hoped operations would show no tendency to ease off at this time. Some of the comments appearing in the press might indicate a more widespread feeling on the down side than was warranted, and it would be a mistake for the Committee to take an action that would indicate a belief that a downward movement had started in the economy.

Mr. Robertson said that he had prepared a statement for this meeting which he now found was generally in agreement with views that had been expressed by others. He then read the statement as follows:

> The present situation is reported to be one of stable to slightly rising total output, with utilization of resources generally high and output close to capacity in some areas. Demands on capital markets continue to be very large. Industrial production is holding about level at the rate that has prevailed since October. However, total expenditures for gross national product apparently will be up in the current quarter, reflecting more largely price increases than growth in real output. In the immediate future, Federal Government spending is scheduled to go up; State and local construction and other outlays are likely to rise at least as rapidly as last year; consumer spending for nondurable goods and services will probably continue to grow. These add up to an impressive total of plusses.
>
> The behavior of some other components of expenditures is more problematical, but there is no evidence at present that any of them is behaving as an important contractive force, or is likely to do so in the next month or so. Plant and equipment spending may rise more slowly, or perhaps level off, in the immediate future, but is unlikely to decline. There are no signs of any substantial shift in business inventory policies that might involve the start of a liquidation movement. Any further declines in residential construction that might occur would undoubtedly not be large enough to be an

important factor affecting the course of over-all activity. Auto sales, after rough allowance for seasonal influences, have been rising somewhat since the introduction of 1957 models.

What this seems to add up to is that output and employment are not changing much at the moment. The pressure of prices is still upward, although more selectivity has been shown lately. No one knows how long this period of relative stability will last. When it ends, no one knows whether the subsequent movement will be gradual or sharp, or which direction it will take. But we do know that supply conditions generally are tight enough that any considerable upsurge in spending would result in aggravated inflationary pressures.

It should be remembered that although GNP has continued to rise over the past year, half of this rise has not represented an increase in real output but rather an increase of prices. It should also be recalled that the upward pressure from wage increases stems in part from general price rises which have been automatically entered into the wage scale for more and more workers under cost of living contracts. Consumer and wholesale prices now are at an all-time high.

Any easing of monetary policy now would be a mistake. The present situation is different from that of the second half of 1956 in that expenditures are not rising rapidly, but what is called for is to hold the line on policy until events make it clear which way the wind is blowing. A brief period of relative stability in total output under the present circumstances does not call for adoption of an easier or expansionist policy. Indeed, such a period is what we need to permit increases in the supply of goods to take pressures off prices and to permit tendencies toward excessive exuberance to be gradually replaced with more realistic planning.

If output continues level over a considerable period, upward pressure is removed from prices, and an appreciable margin of unused resources begins to develop, then an easing of policy will be appropriate; but that situation has not yet arrived. If the economy again breaks out on the upside from a period of stability, further tightening will be called for.

The direction in which the economy is tending will become clearer in the next few weeks as we move out of the confusing early period of the year. Many of the bearish predictions now voiced are reminiscent of those that were prevalent in early 1956. In early March we will have the results of another survey of expected business spending for plant and equipment that will include data on expenditures expected in the second quarter of the year and for the year as a whole. This will give an indication whether such spending is or is not leveling off. Preliminary findings of the survey of consumer finances will be available near the middle of March. Borrowing from banks around the March tax date is an important piece of information. Whether the economic situation calls for a change in monetary policy should be considerably clarified by the developments of the next few weeks.

Our experience last year, it seems to me, illustrates the dangers involved in assuming that we ought to hasten to ease policy when there is a temporary letup in expansion or a bearish period in market psychology. With the advantage of hindsight, it is clear that we should not have eased in January or May. Rather, if we had maintained a steady and tight policy through those short periods of uncertainty, we would have made a more adequate contribution to limiting inflation last year. I think that the same considerations apply now. We cannot effectively curb inflationary developments if we adopt a policy of easing every time there is a temporary lull in an expansion or every time expectations of expansion in future months become something less than unanimous. Furthermore, in view of the degree of inflation already accomplished, every effort should be made to hold the line now against further inroads.

Therefore, it seems to me that we ought to aim at holding to about the degree of restraint that we had last fall, and that we have been aiming for recently but not achieving. Net borrowed reserves should be held to between $200 and $400 million, in the absence of market developments which definitely indicate the need for a departure from this target.

In the same breath I should add that errors should be made on the restrictive side of the range for the next two weeks in order to permit an easing of our policy somewhat in early and mid-March if a potential credit squeeze develops. There are varying opinions on the size of corporate demand for credit for tax purposes on March 15, but it appears that such demand will be substantial and exert pressure on money markets. Considerable liquidation of Government securities by corporations can also be expected then. On top of this demand for funds, the Treasury may have to borrow more new money, or to borrow earlier than had been expected. Even with the addition of $200 million per week through increases in the bill offering, the Treasury may still need additional funds to get through early March, and, in any case, will probably have to borrow in early April.

System action cannot completely offset or guard against the development of such a squeeze but the effects can be spread out somewhat by maintaining a tighter policy now; we would be better able to ease up in March, if necessary to alleviate any credit squeeze that might develop and provide any needed aid to the Treasury, without creating conditions that might contribute to renewed inflation.

Mr. Mills said that the evidence before the Committee had not revealed any clearly defined trend in the economy that would warrant a change from a policy of credit restraint. As usual, there was the question as to what degree of restraint should be applied through the System account. Even more than usual, it was his opinion that the members of the Committee should confine their thinking and their recommendations to the short interval between today and the next meeting of the Committee and not attempt to project their thinking on policy beyond that period.

There was with the Committee again the question what bench mark should be chosen on which to tie policy action, Mr. Mills noted, adding that the general trend of thought expressed seemed to lodge on a level of negative free reserves of $250 million more or less. He had been impressed with Mr. Hayes' statement regarding the desirability of following closely the trend in commercial and industrial loans of banks, and he suggested that the trend of these loans might be a prime bench mark around which to develop the Committee's thinking during this next period. Mr. Mills' thought was that if there was a definite further contraction in the volume of commercial and industrial bank loans, that contraction might be fixed upon as the clearest straw in the wind for indicating policy actions. If commercial and industrial loans tended to contract further, doubt would be raised whether in the face of such contraction it would be advisable to offset the easing effects of the contraction which could happen if the objective of policy was to maintain some fixed level of negative free reserves. Continued contraction in these loans would suggest a change in the economy against which it would be illogical to assert an aggressive policy of credit restraint. On the contrary, such a trend might suggest as Mr. Hayes had indicated that the Committee should allow natural easing forces deriving from the changes in loans to assert their influence on reserves.

Mr. Mills said he did not believe a change in the discount rate should be considered at this time, and he doubted that the situation called for any change in the Committee's directive. The Committee should not be overly influenced by market conditions that might bring the yield on Treasury bills continuously below the discount rate where that falling off in yields might be a market phenomenon and not a phenomenon associated with the availability of bank reserves. In fact, a good case might be made that the softening in bill yields was a reflection of the absorption of bills into hands that would not be of a permanent character and, in consequence, a supply of bills might come back into the market at a later date. However, that might not transpire if new securities issues continued to receive a good market reception and their proceeds were then invested in Treasury bills that came out of the holdings of previous borrowers on the capital market who were then finding a need for cash expenditures on their projects. In that event, no great change in the demand for Treasury bills might occur.

Mr. Vardaman made a statement in which he said that he was largely in agreement with the general views that had been expressed this morning. He felt that it might be necessary to observe the situation for a period of several weeks, perhaps for two or three months, before the Committee could be sure which way activity would move from its present level. Under the circumstances he suggested that the Committee make no change in policy at this time.

Mr. Leach reported that a meeting of the branch and head office directors of the Richmond Bank had been held last week at Charlotte and while he had been unable to attend because of illness he had received a report of the views expressed at that meeting. These views revealed no new elements of strength in the Fifth District economy and pointed to a possible slackening in the rate of advance in aggregate activity with some narrowing of profit margins. The textile industry now seemed unable to escape far-reaching adjustments which appeared to be due in 1950 but which were postponed by Korea. Specifically, capacity in that industry must be reduced by the elimination of marginal producers. The furniture industry was reported to be running below a year ago and cutting into order backlogs. On the other hand, shipbuilding and bituminous coal continued to enjoy a favorable outlook.

Such limited information as had come to his attention regarding sales of new model automobiles indicated to Mr. Leach that dealers were willing to give substantial price discounts as a means of maintaining sales at the current rate. He reported specific instances, stating that while the discounts were not uniform they ranged as high as $600 to $700 on medium priced automobiles, at least as high as the discounts being given a year ago when sales competition was very sharp.

As to credit policy, Mr. Leach felt that economic developments clearly did not call for any increase in restraint at this time. The only question seemed to be whether the System might appropriately decrease the degree of restraint. Despite the growing weakness in certain sectors, Mr. Leach did not believe the System should relax its restraint. This would mean, of course, no change in the discount rate. He went on to say that he believed now, as he had indicated at the preceding meeting, that the latter part of clause (b) of the first paragraph of the Committee's directive calling for recognition of unsettled conditions in the money, credit, and capital markets and in the international situation might well be deleted. It had been inserted in the directive for a special purpose and that situation seemed to have passed.

Mr. Leedy said that his conclusions were much the same as those expressed by others. He felt that we were still in a period when it was particularly difficult to appraise the current situation and prospects. Since the next meeting would take place only two weeks hence, he would continue during that period the policy that had been followed during the past three weeks. Mr. Leedy said that he would be apprehensive regarding Mr. Hayes' suggestion that it might be wise not to take action to counteract a moderate easing of the banks' reserve position should that be caused by further declines in total loans and investments. A sufficient level of net borrowed reserves should be maintained to make clear that present policy was being continued. After commenting on projected reserve figures, Mr. Leedy said that he would not wish to have too much tightness develop in the next two weeks. He would suggest no change in discount rate. At the preceding meeting he had noted a change in atmosphere in the capital markets, and he had then suggested a change in the wording of clause (b) of the directive that called for recognition of unsettled conditions. He still felt some change might be desirable to recognize that conditions had changed since the words were placed in the directive.

Mr. Allen said that Seventh District capital goods lines such as industrial and construction machinery and railroad equipment continued to operate at peak levels. Automobiles and trucks, farm machinery, and consumer durables such as televeision and certain appliances, were well below previous highs. Material "shortages" appeared to be confined to the heavy steel products used in capital goods, that is, structurals, pipe, and plate.

Mr. Allen reported in some detail on current views of leaders in the automobile industry, stating that sales of the 1957 models were now estimated at 6.2 million by the optimists, at 6 million by the realists, and 5.8 million by the pessimists. One leader in the industry had expressed the belief that the used car situation was deteriorating and currently was in worse condition than in many years. He had described his feeling as representing "an informed sense." This leader's standing was such that Mr. Allen felt his sense of things automotive was worth noting.

In view of the importance in the Seventh District of the automobile, farm machinery, and consumer durable goods industries, Mr. Allen said it was understandable why non-farm employment in that area had not shown the rise recorded nationally: 14 of the 24 major labor markets in the area had moderate or substantial labor surpluses with unemployment of 3 per cent or more in January, compared with 7 areas in January a year ago. Consumer demand remained strong and January sales of department stores, retail chains, and mail order firms topped year ago figures commensurate with the increase shown nationally. Their inventory situations were reported as good to excellent. Business loans at leading banks in the district increased slightly in the week ending February 6 after five weeks of decline, but were 4 per cent below January 1. A year ago the decline in the corresponding period was 2 per cent.

In Mr. Allen's opinion, the continued strong consumer demand provided a bulwark against contractive forces and it could provide a basis for expansive forces as the year developed. Although an increasing segment of business sentiment was mildly pessimistic, he did not feel that recession was yet evident or on the way. It was in order to mark time from the standpoint of monetary policy and to remain alert to developments. This would apply to the discount rate, to the degree of restraint at which the Committee had aimed, and to the wording of the directive.

After noting that outdoor activity was at a seasonal low in the Ninth District, Mr. Powell reported on the agricultural situation, which he described as quite satisfactory. Farm land prices had continued to rise during the second half of 1956. Moisture conditions had been improved recently by heavy snows in the western part of the district, and the outlook for spring crops from that standpoint was fairly satisfactory. Prices of farm products in the Ninth District averaged about 6 per cent above a year ago, he said, reflecting particularly a 40 per cent rise in prices of hogs, with prices for none of the major Ninth District products showing a reduction over the past year. In urban areas the economy was in a healthy condition generally with bank deposits in January about 7 per cent higher than a year ago. Department store sales were continuing to increase although at a slower rate than somewhat earlier. Employment in manufacturing industries was running 6 to 7 per cent ahead of a year ago and average earnings of factory workers were higher than in January of last year. Mr. Powell noted a less favorable factor in the recent increase in borrowings of city banks from the Reserve Bank during the past few weeks. This was not a result of increased loans but rather a sharp loss of deposits by those particular banks. The banks were making adjustments to this situation but would continue to borrow from the Reserve Bank for several weeks. Nationally, Mr. Powell agreed with the apparent consensus as to the economic situation and credit policy called for, stating that he could see no reason for reducing the degree of restraint at the present time although he felt the System must watch economic trends closely and be prepared to move whichever way seemed to be called for. At the moment he would make no change in either the directive of the Committee or in the general objectives for net borrowed reserves.

Mr. Mangels stated that reports covering January indicated that Twelfth District economic activity was continuing about as he had reported at recent meetings. Employment in the apparel industry had declined rather sharply, with a larger decline reported in the number of hours worked. A further decline had also occurred in employment in the lumber industry. Aluminum plants were receiving less electric power because of reduced supplies of water for generating electricity in the Pacific Northwest, and output of aluminum was being reduced somewhat, tending to bring a better balance between demand and supply. Automobile sales in California during January were about 10 per cent below a year ago. Over-all construction continued at fairly high levels with no recent changes in either residential or non-residential activity. Bank loans had declined during the past three weeks and borrowings at the Reserve Bank were very nominal. Twelfth District banks continue to be net lenders in the Federal funds market.

Mr. Mangels reported on further checks that had been made on the expected demand for tax borrowings in the Twelfth District, stating that most of the banks do not anticipate any large increase in corporate demand for credit for that purpose this year.

As to credit policy, Mr. Mangels said that even though available data did not indicate significant changes in activity during the past few weeks, there was some indication that the economy might currently be moving toward better equilibrium. He would not suggest a change in policy at this time but would aim for negative free reserves somewhere around $200 million, and would not go much over that figure; he would not change the discount rate; and he would be inclined to leave the directive unchanged at this time.

Mr. Erickson said that economic conditions in the First District did not differ from the excellent presentation that had been given by Mr. Young. Nonmanufacturing nonfarm employment was up in December over November. Most manufacturing industries were up except for textiles, where the situation was not good. Production of shoes in 1956 had been of record proportions but was now "in between" seasons, and this period of reduced output was running a little longer than usual because of the late date of Easter this year. Department store trade was good.

Mr. Erickson said that he would make no change in the discount rate at this time and he would not change the directive of the Committee even though the unsettled conditions in the money, credit, and capital markets that had been discussed in December might not be quite as unsettled as at the time the directive was last modified. He would continue the policy of restraint through open market operations.

Mr. Szymczak said that the next two weeks might offer a good period in which to spot check the situation in various districts to the extent possible. He did not think it a time for any change in policy: any change at this time might hurt rather than help the economy, and any easing might indicate that the System felt activity was about to turn down. The System should be mindful of Treasury needs and should go along with those needs. Mr. Szymczak suggested that a negative free reserves position in the $200-400 million range would seem appropriate between now and the next meeting of the Committee.

Mr. Balderston said that the rolling adjustments that had characterized the economy in recent years seemed to be continuing at this time. On the one hand, he sensed less ebullience, some consumer price resistance, and the probability of a leveling off in factory construction and in manufacturing inventories. He noted that some insurance companies had experienced a drop since November in applications for conventional mortgages. On the other hand, Government spending at both national and local levels was certainly on the increase, and fiscal policy would probably not lend as much support to monetary policy in the future as it had in the recent past. Mr. Balderston said that he would like to see the Committee regain the restraint it had attained last fall until the situation became more clear. As to the Committee's directive, he felt there had been a reason at the time for inserting the instruction in clause (b) to recognize unsettled conditions, and he raised the question when the clause would be removed if it were not taken out at this time.

Chairman Martin stated that he had just completed ten days of travel during which he had talked before groups in Florida, Texas, and Iowa and while he recognized that impressions gained on these "travelogues" were not in any sense conclusive he felt it might be worth while to comment on those he had gotten during this period. There was no question, he said, but that business sentiment had changed and that there was not the optimism that existed six weeks or two months ago. This was fairly general. In Florida, he had noted less optimism even in areas where new hotels were going up, despite the fact that the tourist season had only begun. Persons in that business in whom he had some confidence had commented, nevertheless, that they expected a "whale of a season" later on. The Chairman said that his over-all feeling as a result of observations in the areas he had visited was one of more confidence of the vitality of the economy than he had had before he started the trip. He felt the Committee should be very wary about permitting monetary policy to get into the position of helping to promote a new bulge. There have been sharp increases in prices in some areas which may well have created a situation that had to be corrected. This condition and some practices that were recognized as unsound by many of those who were engaging in them would not be corrected by an easing of monetary restraints.

Chairman Martin went on to say that the consensus at this meeting seemed clear in calling for continuation of the status quo. On the directive, while he had no strong feeling about it one way or the other, he felt that the international situation to which reference was now made in clause (b) was no better than at the time the reference was inserted in the directive, and it might be worse. There had also been generated some talk of depression by remarks of the Secretary of the Treasury and former President Hoover as well as by others. Currently the Treasury's balance was low and the outlook for receipts was very uncertain at this time. It might well become necessary for the Treasury to borrow directly from the System, although he hoped this would not develop. In view of these developments and of the many cross currents in the situation, it did not seem to him necessary to eliminate the reference to unsettled conditions in the directive at this time. On the whole, his feeling was that it might be continued in its present form since the next meeting would be held only two weeks away. Specifically, he suggested that the Committee maintain the status quo with the understanding that the minutes would reflect the different degrees of emphasis that different individuals had suggested this morning, and that these be used by Mr. Rouse as a guide in carrying on operations during the next two weeks. He then called upon Mr. Rouse for comments.

Mr. Rouse said that he felt he understood the various views expressed this morning. He commented on the projections of reserve funds during the next few days and stated that the System account might be in a position of buying securities shortly.

Mr. Hayes noted that if the System's maturing bills were permitted to run off, its bill portfolio would decline to approximately

$100 million. Mr. Robertson inquired whether Mr. Hayes felt this would be undesirable, and Mr. Hayes responded that it would be undesirable only in the sense that if the System had only $100 million of bills, and if it wished to make sizable sales of securities for the purpose of absorbing reserves quickly, such a move would be more difficult to accomplish than if the System had larger bill holdings.

Mr. Rouse agreed with this comment. He then raised the question whether the Committee felt that transactions in short-term securities other than bills should be made only on the sell side, or whether in the event the System wished to put funds into the market it might purchase short-term securities other than bills. He added that System account operations might help to broaden the market for these short-term securities if transactions were entered into on both sides of the market.

Mr. Mills stated that he felt purchases of securities other than bills would raise a very fundamental question. Such action would cause very serious misgivings on his part, and it might lead to confusion in the market. Mr. Mills hoped there was a clear understanding that the selling of certificates and notes was for the purpose of absorbing reserves and that when it became necessary to supply additional reserves and Treasury bills were available, there would be no move to buy back certificates or notes that had been disposed of.

Mr. Robertson said that he had the same views as those expressed by Mr. Mills.

Mr. Hayes commented that his off-hand thought was that the System might wish to rebuild its bill holdings.

Chairman Martin said that he did not think the Committee at any time had intended to put reserves into the market by purchasing Treasury notes or securities other than bills.

Mr. Hayes then stated that he would also like to make an observation for the purpose of keeping the record straight as to the references made earlier in this meeting to lack of tightness in the market in recent weeks. The fact is, he said, that in the three weeks ending February 13 there was an average net borrowed reserve figure of $236 million, which was in the $200-300 million average that had been suggested at the preceding meeting. It was true that in the first three weeks of January positive free reserves existed. The tone of the market recently may not have confirmed the figure of negative free reserves, but Mr. Hayes said that he wished to call attention to the fact that operations had attained the figures that the Committee seemed to have in mind.

Chairman Martin stated that he was glad Mr. Hayes had brought out this point, adding that this was the thought back of his comment when he asked Mr. Bryan earlier in the meeting whether the ease he (Mr. Bryan) had referred to recently was in his judgment "inadvertent" or "overt." Chairman Martin said that it seemed clear that the ease that had been referred to was not overt.

Mr. Vardaman said that he had understood the selling of certificates and notes recently was brought about because bills were in short supply, and he inquired whether it was clearly understood that the System was not going to buy back any certificates or notes if any bills were available for purchase when funds were to be put into the market.

Chairman Martin stated that he assumed this was clearly understood, and none of the Committee indicated a different view.

Mr. Rouse stated that he had raised the question because he wished to clarify the matter, and the Chairman said he thought it important to have that point clarified.

Mr. Shepardson returned to the Chairman's comments on the consensus, stating that he hoped that errors in carrying on operations during the next two weeks would be on the side of tightness rather than of ease.

Chairman Martin replied that he did not think any purpose would be served in taking a vote on this question and that this was why he felt the record of the discussion should be used by the Management of the Account as a guide to carrying out its operations during the next period.

Mr. Thomas noted that during January credit was being liquidated very rapidly during the period when "ease" was indicated in the market, in terms of some positive free reserves. He pointed out that it was not necessary to add to tightness in order to carry out the Committee's objectives when the liquidation of bank loans was accomplishing what the Committee desired. The ease referred to in January, he said, was not because the System was not carrying out a restrictive policy but resulted entirely because credit was being liquidated very rapidly.

Chairman Martin stated that this was correct and that he was glad this point had been brought out. There was no point in trying to pursue a more restrictive policy if the objectives were being carried out.

Chairman Martin then turned to the directive to be issued to the Federal Reserve Bank of New York, stating that if there was no objection the directive would be renewed without change in the wording. In response to the Chairman's question, Mr. Rouse stated that he would suggest no change in the limitations contained in the directive and that if anything developed to make it necessary he would come to the Committee for additional authority.

> 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:

> (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, while recognizing unsettled conditions in the money, credit, and capital markets and in the international situation, 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 stated that the next meeting of the Committee would be held at the time tentatively agreed upon, that is, at 10:00 a.m. on Tuesday, March 5, 1957, noting that this would be the annual organization meeting of the Committee.

The Chairman also stated that he had received word from Mr. Sproul that he would be in Washington on March 4, 5, and 6, and that he hoped all of the Presidents and others who knew Mr. Sproul would plan to attend a luncheon to be given for him in the Board's dining rooms on March 5.

Chairman Martin also noted that the Special Committee that had been appointed for the purpose of studying the questions raised by the suggestion made by Mr. Mills at the meeting on January 8 would hold a meeting today.

Thereupon the meeting adjourned.

Winfield W. Riefler
Secretary