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, December 17, 1957, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Hayes, Vice Chairman
Mr. Allen
Mr. Bryan
Mr. Leedy
Mr. Mills
Mr. Robertson
Mr. Shepardson
Mr. Szymczak
Mr. Williams

Messrs. Fulton, Irons, Leach, and Mangels, Alternate Members of the Federal Open Market Committee

Messrs. Erickson and Deming, Presidents of the Federal Reserve Banks of Boston and Minneapolis, respectively

Mr. Riefler, Secretary
Mr. Thurston, Assistant Secretary
Mr. Sherman, Assistant Secretary
Mr. Hackley, General Counsel
Mr. Solomon, Assistant General Counsel
Mr. Thomas, Economist
Messrs. Atkinson, Bopp, Marget, Mitchell, Tow, and Young, Associate Economists
Mr. Rouse, Manager, System Open Market Account
Mr. Carpenter, 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. Ellis, Hostetler, Daane, Roosa, and Wheeler, Vice Presidents of the Federal Reserve Banks of Boston, Cleveland, Richmond, New York, and San Francisco, respectively; Mr. Parsons, Director of Research, Federal Reserve Bank of Minneapolis; and Mr. Walker, Economic Adviser, Federal Reserve Bank of Dallas

Chairman Martin stated that the minutes for the meeting of the Committee held on December 3, 1957, were not being presented for approval at this time because the members had not all had an opportunity to review the preliminary draft and suggest changes. However, he noted revised pages of the minutes for the meeting held on November 12, 1957, reflecting the discussion of those minutes at the meeting on December 3 had been distributed. The Chairman inquired whether all members of the Committee had had an opportunity to read these revised pages and whether there was any suggestion for further change. None of the members indicated that they wished to suggest further changes in these minutes.

Thereupon, upon motion duly made and seconded, the minutes of the meeting of the Federal Open Market Committee held on November 12, 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 December 3 through December 11, 1957, and a supplemental report covering commitments executed December 12 through December 16, 1957. Copies of both reports have been placed in the files of the Federal Open Market Committee.

Mr. Rouse reported that dealer positions and the funds required to finance those positions had built up to a high figure. About $1.8

billion of Government securities were now held by reporting dealers, exclusive of about $300 million of securities out on special repurchase arrangements. Positions had fluctuated in the neighborhood of a billion dollars prior to the discount rate change, but the Treasury financing in the last half of November added to dealer holdings of bonds, notes, and certificates. Before the dealers were able to work off those positions, a large volume of tax swapping developed involving switches from shorter to longer maturities, and a large part of the short securities brought into the market on this swapping had remained in dealer positions. The bulk of dealers financing had fallen on the New York banks, Mr. Rouse said, with the result that their basic position moved from a surplus a week or so ago to a deficit of about $400 million by Friday, December 13.

The December liquidity need that centered on the New York banks and on dealer positions had created a tight situation in the short-term Government securities market, Mr. Rouse stated, and Treasury bill rates, which had fallen below the discount rate, had been rising during the past few days. The new bill auctioned yesterday went at an average rate of almost 3.15 per cent. Dealers were awarded more than $300 million of the new bills, which was in addition to the 3/4 of a billion dollars of bills that they already held. Mr. Rouse said it was clear that the Government securities market had a distribution problem ahead; moreover, the past record showed that dealer positions would tend to build up further over the next two weeks.

Mr. Rouse went on to say that reports from the capital market after the change in the discount rate suggested that market supplies of Government, corporate, and municipal securities were quickly cleared up. It seemed likely, however, that these markets were giving an appearance of greater strength than they actually possessed. Some of the buying that had driven interest rates so rapidly lower had represented "one-shot money," and some buying reflected dealer takedowns of new securities for speculative purposes. He thought it interesting to note that, while bank loans on securities other than U. S. Governments had not increased since the discount rate change, neither had they been reduced, and loans on Governments had increased.

Turning to the matter of Treasury financing, Mr. Rouse reported that the only firm information he had was that the Treasury planned to continue adding $100 million to each of the next five weekly bill issues, and it also planned to roll over the $570 million of maturing Fanny May notes through the Federal Reserve Banks in January.

At the conclusion of Mr. Rouse's report, Mr. Allen asked for an explanation of the remark that the Treasury would roll over the FNMA notes through the Federal Reserve Banks. Mr. Rouse replied that these are mortgage liquidation notes and that the offering and distribution of these securities is handled through the Reserve Banks.

Mr. Erickson suggested that nonbank investment demand for short-term Governments ordinarily builds up after the year end so that the present large dealer positions might be worked down then, to which Mr. Rouse replied that this was the typical seasonal pattern.

> Thereupon, upon motion duly made and seconded, and by unanimous vote, the open market transactions during the period December 3 through December 16, 1957, were approved, ratified, and confirmed.

At Chairman Martin's request, Mr. Young summarized in the statement presented below the current economic situation, which had been more fully reviewed in a staff memorandum dated December 13, 1957, on Recent Economic and Financial Developments in the United States and abroad. A copy of the staff memorandum, which had been distributed before this meeting, has been placed in the Committee files.

> In recent reports to the Committee, I have used the words "down-settling" to characterize the drift in over-all activity. In the light of recent information, general economic recession now appears to be the most appropriate description.
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> Industrial production for October has been placed one index point lower than earlier reported, namely, at 141 instead of 142, and for November the preliminary estimate is 139, or down three index points in a month and five index points from the September level of 144. Declines in October were fairly widespread, including durable, nondurable, and mineral sectors, and preliminary information suggests that a pattern of fairly widespread decline was repeated in November. In durable goods output, November auto assemblies were a strong factor on the upside, but not strong enough to offset the minuses. A resistant sales market in November is resulting in somewhat reduced assembly schedules for December.

A second bit of news justifying a characterization of general recession is that relating to business plant and equipment expenditures. The latest Commerce-SEC survey projects a spending rate for the first quarter of 1958 five per cent under the current quarterly rate. This either means that the decline in such spending, projected by the McGraw-Hill survey, is coming faster than earlier anticipated, or that the downward adjustment in plant and equipment is destined to be greater than the McGraw-Hill survey implied.

Inventory developments in October constitute a third item of evidence pointing to general economic recession. Liquidation in total business inventories in October was at $4.5 billion annual rate, almost entirely concentrated in durable goods lines. Business sales in October fell off faster than inventory liquidation so that the over-all stock-sales ratio rose, reaching the highest level since the spring of 1954. Stock ratios have become particularly high in durable goods lines at manufacturing levels. Judging from data that ordinarily correlate closely with changes in business inventory holdings, November also was a month of over-all inventory liquidation.

Reports from the labor market also point to general recession. Reductions in employment from mid-October to mid-November were widespread and sizable in nonmanufacturing as well as manufacturing, and unemployment rose to 3.2 million--about half a million higher than a year earlier. On a seasonally adjusted basis, unemployment reached approximately 5 per cent of the civilian labor force, or the highest rate since late 1954. Since mid-November, initial unemployment compensation claims filed have continued to run well ahead of a year ago. The length of the work week in manufacturing dipped further in November and at 39.2 hours was a full hour less than a year ago; reductions occurred in both durable and nondurable lines.

Reflecting easing employment conditions, personal income was off again in November for the third successive month. From the seasonally adjusted annual rate of $347 billion in August, the November rate was down about $3 billion. Reduced personal income was apparently of some influence in retail trade, which fell one per cent each in both October and November, with declines concentrated in durable goods lines. Declining personal income is also thought by some to be a factor in December retail markets, although bad shopping weather and transit strikes in some major metropolitan areas are also obvious factors in disappointing sales for this season of the year.

The declines in output, employment, and activity evident in recently reported data imply a fourth quarter reduction in over-all performance of the economy, as measured by GNP. Preliminary estimates for the fourth quarter now place GNP as down 1 per cent or $4 to $5 billion, annual rate, from the third quarter--the first decline in three years.

Wholesale price changes have been fewer and smaller in recent months than earlier, so that the average of wholesale prices has been showing little change. There are two schools of thought on this development. One is that wholesale commodity demands over-all, though contracting some, continue strong enough to support current wholesale price levels, particularly with the appreciable downward adjustments that have already occurred in primary materials prices. The other school questions the sensitivity of existing price indexes, particularly for the area of finished goods, and wonders whether pressures of competitors to sell are not resulting in under-the-counter concessions and discounts, not yet registered in price quotations recorded for price index making. In any case, the price situation is not clear, as has been the case at other points of turn in business conditions, and close scanning of market price developments will be called for in the period ahead.

In markets for consumer goods, prices of meats have been rising again, and there have also been price advances for new autos, some appliances, and apparel. These advances, together with further price rises for services and rents, probably spell some further modest rise in the consumer price index for November, and possibly for December too, following a pause in October.

Abroad, contractive developments in economic activity appear fairly clear in Canada, but in industrial countries of Western Europe the indications of recently available data are mixed. Aggregate industrial production in this area declined slightly from the second to the third quarters and apparently further in October. Recent international trade data seem to show more indications of decline than expansion. But monetary policies in important countries of Western Europe continue on the relatively restrictive side, suggesting that inflationary dangers and balance of payments disequilibria are still given heavy weight in the highest councils of financial policy. In other areas of the Free World, problems are diverse, but the significant facts all point to a much slower pace of advance in physical activity than earlier, and with reduced levels of raw material prices, some reduction in the current value of international trade for various countries supplying such materials.

While contractive tendencies have recently been dominant in this country and in Canada, with leveling out tendencies abroad, it is important to remember that levels of activity generally are still high. Whether recession domestically will be moderate and short-lived, and internationally limited or relatively confined, cannot be foretold at this stage. The major problem of this cyclical topping and recession seems to be digestion of new capacity to produce rather than of absorbing too optimistic inventory accumulations. This may make considerable difference in the nature and duration of this cyclical adjustment. However, underlying forces of economic growth and technological advance still appear to be very strong, and these forces can be counted on to moderate the adjustment process.

There was a brief discussion of Mr. Young's comments, particularly of gross national product and of the relationship between inventories and gross industrial production, after which Chairman Martin called upon Mr. Thomas, who then summarized recent financial developments, which also had been reviewed in the staff memorandum of December 13. During his comments, Mr. Thomas referred to an additional memorandum on the Outlook for Treasury Cash Requirements and Bank Reserves which had been sent to members of the Committee under date of December 13.

Financial markets in the past two weeks have continued to adjust to the conflicting forces of the more or less psychological impacts of the discount rate reduction and the changed economic outlook on the one hand and the realities of the current money market situation on the other.

The decline in interest rates in the past month has probably been the sharpest on record. Yields of some bonds have declined as much in this brief period as in several months in 1953. Within the past week, however, the bond market has tended to level out, and some yields have risen.

Bill yields, after dropping to below the discount rate, have firmed and are now closer to 3-1/8 per cent. The stock market has been generally weak.

Among the current realities that have helped to check the decline in interest rates are (1) the continued fairly substantial volume of new issues of securities; (2) the usual mid-December liquidity demands, which result in offerings of Treasury bills and increases in bank loans; (3) distribution of the latest new Treasury issues; (4) the $100 million increase in the weekly Treasury bill offering; and (5) the exceptionally large positions of dealers in Government securities. Holdings by dealers, which were already heavy, have been increased to such high levels that dealers are now hesitant about buying more offerings and are having difficulty in financing their positions.

These are all temporary factors that have little significance with respect to broader trends but which exert immediate pressures on the market. While some slowing down in the precipitate rate of decline in interest rates may be desirable, these temporary forces need not be permitted to create roadblocks to prompt adjustment of markets to the broader factors. If a serious downturn in economic activity is to be avoided, funds should be freely available for potential borrowers who would put them to use.

Review of estimates of Treasury needs indicates the likelihood of somewhat larger borrowing demands from that source during the next few weeks than had been anticipated. An additional $100 million each of the next six weekly bill issues will probably not be adequate to meet cash needs of the Treasury, and as much as $1 billion more may have to be borrowed in February. Our latest estimates, revised in light of the current business downturn and trend of expenditures, indicate an excess of cash expenditures over receipts of about $1 billion for the current fiscal year, compared with a cash surplus of $3 billion shown in the official budget review of last October. The calendar year estimates are also for a deficit of $1 billion in 1958, after a $2 billion surplus in 1957, and $5.5 billion surplus in 1956.

This shift from surplus to deficit results principally from increased expenditures. Prospective receipts show moderate increases over past results, although they fall short of previous forecasts. These results and prospects show how much the Treasury position is shifting from an anti-inflationary posture to a stimulating or at least sustaining one for the economy. They present problems, however, for the Treasury with respect to the debt limit and the timing of borrowing operations. The Treasury also faces the problem of longer-run significance of taking advantage of the strong bond market to extend maturities of the debt. This is particularly important in view of prospective and perhaps growing deficits.

Banking figures for the past two weeks show a shift from contraction to expansion. This shift reflects in part bank subscriptions for the new Treasury issues in the week of December 4 and in part seasonal loan demands to meet December liquidity requirements by businesses, both financial and nonfinancial. Using partial data for December 11, it appears that total loans and investments of banks in leading cities, excluding interbank loans, increased by about $1-1/4 billion in the past two weeks compared with only about $300 million in the same two weeks last year.

Commercial and industrial loans at these banks increased by nearly $300 million in the latest two weeks, compared with a little over $400 million in the same weeks last year. Bank loans to dealers in securities increased by nearly $300 million this year, against a rise of only $70 million in the same period last year. This difference reflects not only the Treasury financing this year but the exceptionally large positions and borrowing needs of dealers in Government securities. Reporting banks' holdings of Government securities increased by $600 million and those of other securities by over $100 million compared with decreases aggregating $270 million in the same period last year.

Demand deposits adjusted at reporting banks have shown a seasonal increase in the past two weeks, but by a much smaller amount than last year. The additional bank loans and investments have gone in part to maintain Treasury deposits, which were being sharply reduced at this time last year. In November demand deposits adjusted showed less than the usual seasonal increase, only partly offset by a more than seasonal increase in currency in circulation. The total money supply is about one per cent less than a year ago.

A particularly significant development in November was a decline in the seasonally adjusted annual rate of turnover of demand deposits at banks outside New York. The rate of turnover has now declined to about the same level as a year ago. Thus it can no longer be said that increased turnover has offset the effect of a decrease or lack of growth in the supply of money.

System operations in late November and early December and a reduction in Treasury balances at the Reserve Banks

> have supplied a substantial volume of reserves to meet seasonal needs. Net borrowed reserves have generally averaged close to or below the $200 million level. In the course of the past week, however, there has been considerable demand for reserves, due in part to a sharp increase in required reserves resulting from credit expansion, as well as to the usual currency needs. The tone of the money markets has shifted from ease to tightness. Although the expected large seasonal increase in float may supply a substantial amount of reserves this week and next, some additional aid in financing dealer positions and supplying reserves to cover liquidity needs seems to be appropriate. Larger amounts will be needed in the week after Christmas, as float declines. Most of these funds might be supplied through repurchase contracts.
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> In January, reserves will be abundantly available from the seasonal return flow of currency and reduction in required reserves. The System account might be reduced by as much as $600 million plus any amounts added in the next three weeks. If net borrowed reserves are kept close to the zero level, additional purchases of about $500 million may be needed this month and sales of $1 billion or more would be appropriate in January.

Chairman Martin said that it was obvious that we had had an interesting month since November 17. This morning the usual go-around would start with Mr. Hayes and would be followed with statements by Mr. Erickson and others. The Chairman noted that this probably would be the last meeting to be held during 1957, and he suggested that it would be appropriate to take a look at clause (b) of the first paragraph of the Committee's directive to the Federal Reserve Bank of New York. However unsatisfactory the language of the directive might be, it was the medium by which the Committee reported its policy actions to the Congress. The Chairman said that he had given consideration to the present wording of clause (b) and had discussed it with Mr. Riefler, who had suggested that the clause might appropriately be changed to provide for transactions with a view "to cushioning adjustments and promoting recovery in the economy by maintaining an ample volume of bank reserves." The Chairman went on to say that he had no brief for any particular wording and that the wording Mr. Riefler had suggested might not be in order, but it was his view that the directive should receive attention in the comments to be made by the individual members of the Committee. He then called upon Mr. Hayes.

Mr. Hayes expressed his views on the economic and credit situation as follows:

> New economic data available since our last meeting tend to confirm the developing recession, which now extends over a fairly broad range of industries, although it is still very moderate in intensity. The decline in industrial production during the past two months now appears to have been greater than was indicated previously. Steel output has slipped further, and automobile production, which reached a high level in November, is scheduled for some reduction this month and may have to be cut further if an excessive accumulation of inventories is to be avoided. The figures in the November Commerce-SEC survey of plant and equipment expenditures suggest a more pronounced over-all decline in 1958 than the 7 per cent drop indicated earlier by the McGraw-Hill Survey. Unemployment now exceeds 5 per cent of the labor force, while average weekly hours worked in manufacturing dipped sharply again in November and may decline further in December.
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> Business inventories declined in October for the first time in three years, and although this was due largely to a temporary reduction in new car stocks prior to introduction of the new models, manufacturers' inventories also showed a small reduction. Even after this decline, the ratio of manufacturers' inventories to sales reached a new high since early 1954.

Revised retail sales data for October are a little better than had been suggested by the preliminary report given at our last meeting. Department store sales showed moderate improvement in November, but automobile sales were disappointing. It may be some time before a clear appraisal of the volume of Christmas buying becomes possible, but the general atmosphere at the moment is not especially encouraging.

Data for all member banks for the three weeks ending December 4 confirm the pronounced lag in business loans which has characterized the second half of 1957. Much of this lag is attributable to smaller borrowings by sales finance companies, but a number of other industry groups have shown smaller borrowings or greater repayments than a year ago. In contrast with bank loans, bank investments rose much more in the last three weeks than a year ago, mainly because of sizable purchases of the new Treasury issues. Since the last meeting we have made some informal checkings with the large New York banks on the causes of reduced loan volume and have found that it is attributed largely to lessened inventory pressures and some actual inventory liquidation, as well as to some shift of demands to the capital markets. A lesser factor may be the tightening of loan standards initiated some months ago, which in many cases has gained momentum just as demands were tending to drop off. Most loan officers feel that business loan demand continues to slacken, although not in any spectacular degree, and the banks still feel "tight" in view of their high loan-deposit ratios. The latest weekly loan figures for New York banks show a considerably greater gain both in business loans and in security loans than a year ago, but this may represent only a repetition of the experience in previous tax periods this year.

Already the recession, such as it is, has forced a considerable revision of our estimates of Treasury revenues, so that we now expect only a very small cash surplus, if any, for fiscal 1958. It appears that $1 to $2 billion of cash will probably have to be raised early in February, or perhaps even in late January, over and above the amount to be realized in the next few weeks from the $100 million increase in the weekly bill issue. We would think it highly desirable that the debt ceiling be increased in January to leave enough leeway for this cash financing.

The sharp declines in market interest rates which were the most dramatic result of the discount rate cut and which were commented upon at the last meeting, have carried a good deal further in the past two weeks. New issue rates on high grade utility bonds are about 5/8 to 3/4 of a percentage point below the level of September and October, while market yields on Treasury bonds are down as much as one full percentage point from the peak of late October. This rapid readjustment of rates has been based in large part on psychological reaction to the shift in System policy rather than upon the actual steps the System has taken to release reserves. It has, of course, been aided by a temporary lull in new security issues and the continued lag in bank loans. Banks have been led to lengthen maturities, and institutional investors have mobilized available funds to buy longer-term corporate and Treasury securities. With borrowers able to sell new capital issues easily and at lower interest rates, the availability of credit has been improved in a very real sense.

These effects of the discount rate cut, taken together with the moderate lessening of pressures on bank reserves, suggest that the Committee has achieved the objective sought at the last two meetings, i.e., an effective change in policy toward less severe credit restraint. With respect to long-term interest rates, the results have exceeded our anticipations, and the rapidity of the rate decline may have made the market vulnerable to unfavorable news or disappointed expectations. To some extent investment demand has been borrowed from the future, and with a heavy calendar of new corporate and public financing still in view, the flow of savings may well prove insufficient to support the present rate structure. In that event, there might be disturbing repercussions in the money and capital markets which might require, at some stage, further System action to encourage bank investment and lending.

We should be on our guard to prevent a turn toward tightening over the year-end period. Certainly the steadily worsening business situation provides justification for our countenancing an easier credit atmosphere than we might have sought a month or so ago.

I think we should try to avoid creating the impression that the System is moving rapidly to a policy of "active ease," but at the same time we should avoid creating the impression that we are doing nothing "real" to ease credit. I would urge that the level of net borrowed reserves be allowed to drift somewhat lower and perhaps approach the zero level in January, provided of course that we give attention also to interest rate developments and the tone of the market. If current projections are anywhere near accurate, only moderate outright purchasing may be required in the next three weeks, repurchase agreements being used to cope with most of the projected bulge in net borrowed reserves for the week ending January 1.

As for the directive, this is our last opportunity to change the wording and have the change included in the published record for 1957. I would feel better if that record reflected a more frank recognition that we have encountered a recession and that our policies are being molded accordingly. I would therefore suggest that clause (b) be rewritten as follows: "to mitigating recessionary tendencies in the economy."

Mr. Erickson said that most of the statistics for the First District continued to move downward. He also reported that at the meeting of directors of the Boston Bank yesterday, two of the directors who are machine tool builders and who have been pessimistic for several weeks were much more pessimistic, and their pessimism influenced their views on the national situation. Manufacturing employment in the Boston District during October was 4 per cent below October a year ago, New England indexes of industrial production showed decreases during October, and department store sales recently had been disappointing. Automobile registrations in September and October were ahead of last year, but dealers report that sales slumped badly in November. The only hopeful thing in the picture was construction which, in October, was ahead of September this year and of October last year, mostly because of increases in public works and nonresidential construction. For ten months of this year as compared with last residential construction was 3 per cent ahead, due primarily to multiple-unit housing.

As to policy, Mr. Erickson would make no change in the discount rates at this time but he felt some change in the wording of the Committee's directive would be desirable. His preference would be for wording such as Mr. Riefler had suggested. In the open market, we were coming to the usual year-end developments, and he would be inclined to leave operations pretty much to the judgment of the Manager of the System Account. If this meant net borrowed reserves around zero, that would be all right with him.

Mr. Erickson said that when Governor Balderston was in Boston last week he attended a meeting at which there was a review of discount operations. It was Mr. Erickson's view that even though the System's posture had changed, it should continue to watch the discount window for continuous borrowing, and Governor Balderston had suggested that at this meeting there be a discussion concerning use of the discount window.

Mr. Irons said that conditions in the Dallas District had shown some tapering. Agricultural conditions were not as favorable as a month or six weeks ago because weather conditions had delayed getting crops in. Reporting on a spot check made yesterday, Mr. Irons said that construction was continuing to move upward slightly and the outlook among those in the building industry was favorable although cautious. Construction was expected to increase slightly rather than sharply, but builders anticipated a small boom in residential activity, particularly in houses in the $8,000-$14,000 bracket. There also were reports of improvement in the availability of mortgage money. Employment recently had declined slightly whereas normally a seasonal gain was expected at this time of year. Department stores estimated that holiday business might about equal last year's. Total bank loans dropped off in the three weeks ending December 11, Mr. Irons reported, reflecting a decline in commercial and industrial loans. Banks report demand for credit, particularly for consumer credit, continues strong. Both banks and department stores have indicated that collections continue good. Conditions in the petroleum industry might be a little better than indicated by some of his recent reports, Mr. Irons said, because of cold weather that had cut into fuel oil stocks and because of cutbacks in production. On the whole, the situation in the Dallas District was tending in the same direction as in the country as a whole, although probably not to the same extent. He found no pessimism but a recognition that adjustments were taking place at a very high level. No one was expecting a large upsurge, but neither was a material decline expected. In the background there was a feeling among businessmen and bankers that deterioration in the Treasury position moving from a surplus into a deficit might have a sustaining effect.

Mr. Irons said he had been pleased with the handling of the System Account during the past two difficult weeks. He had hoped it would be possible to come close to a rate structure appropriate to a 3 per cent discount rate, and this had been done with bill rates fluctuating around 3 per cent. The market had not been unduly tight but neither had it been excessively easy; there had been about as much restraint as could be expected under a 3 per cent rate structure. Mr. Irons would hope that in the next three weeks the account could operate similarly. He did not think that industrial production would be gotten up by pumping in the money. He still thought the prices of Government securities might in the future pose some problems that would not have been present if prices had not risen as sharply as in the past few weeks. He hoped the System would continue to provide reserves that would be reflected by rate conditions and structure around the 3 per cent discount rate. He would give considerable leeway to the Manager of the System Account and would expect him to operate by feel almost on a day-to-day basis. However, excessive ease should be avoided because that would come back to plague us if a too easy situation were created.

Mr. Irons said he did not like the directive that the Committee had. It seemed to him that it forced continued cumulative action. He would prefer to leave out any reference to moderating pressures on bank reserves or to assuring adequate reserves and would change clause (b) of paragraph 1 more along the lines Mr. Hayes had suggested so as to call for operations with a view "to maintaining conditions in the money market that would tend to mitigate recessionary tendencies."

Mr. Mangels said that the Twelfth District picture continued mixed with further moderate declines in production. Department store sales were somewhat disappointing. Automobile sales had been holding up pretty well but dealers report considerable price cutting with substantial effect on profit margins on both 1957 and 1958 models. Preliminary information on employment in California and Washington suggested no change in November from October but insured unemployment was up 80 per cent from November 1956. Agriculture was in pretty good shape with large wheat and apple crops but with prices down. The California and Arizona cotton crops were very good with yields of 1,000 to 1,100 pounds to the acre or about 2-1/2 times the national average. Construction figures were holding up well. Twelfth District bank loans during the past two weeks had declined slightly and an analysis of 28 reporting member banks showed that loans of 12 of these on December 4 of this year were below a year ago, while 16 were higher. One large San Francisco bank had expressed the view that demand for loans, particularly for business loans, was somewhat less than it had been, and payoffs were being made in December instead of January. Other San Francisco banks report continuing demand for business loans and expect no more than a seasonal decline after the year-end. Demand deposits had declined recently contrary to the national picture, but savings deposits had increased three times as much as in 1956. Borrowings by member banks from the Reserve Bank were nominal.

Mr. Mangels thought the next few months probably would continue to show the business situation deteriorating, but the worst might be over so far as expectations were concerned. Adjustments were occurring and, while there was full recognition of the present situation, he sensed some degree of optimism so far as the picture for 1958 was concerned. His thinking would be that open market operations should aim for around $100 million of negative free reserves, certainly not over $200 million, during the next few weeks. He had in mind changing clause (b) of paragraph (1) of the Committee's directive to call for operations with a view "to regulating the supply of bank reserves so as to foster sustainable growth in the economy without inflation." However, for the record he thought the suggestion by Mr. Hayes was preferable to the one he had had in mind.

Mr. Deming said that national statistics pointed to a downturn still reflected imperfectly in the Ninth District. Certainly the slope of the decline was more pronounced at the national than at the district level. November nonfarm employment in the district was down 18,000 from October, somewhat greater than seasonal. Manufacturing employment was off 6,000, mostly contraseasonal, with declines in most categories. On the other hand, construction employment had dropped by less than the usual amount. Mr. Deming recalled that he had mentioned before that the Ninth District seasonal high in unemployment usually comes in late January or February. This coming winter, it is now expected to occur a little earlier, to be higher, and to last longer.

Bank debits in November were 2 per cent less than a year earlier, Mr. Deming said, and department store sales were off 5 per cent. In the week of December 7, however, department store sales were even with the comparable week of 1956 for the first time since late October. New passenger automobile registrations in the Twin Cities in November were 11 per cent higher than last year and were running about 3 per cent ahead of last year in the first ten days of December.

Banking figures show continuation of the recent trend with smaller than usual deposit gains or higher than usual losses, Mr. Deming said. Loans also had declined in the Ninth District. Mr. Deming said that he had looked further into the question of demand for commercial bank loans since the December 3 meeting and that the reduced loans reflected a diminished demand more than commercial bank policy. However, the banks were not unhappy with these developments. The easier credit picture was being reflected in easier mortgage credit with one Twin City bank now actively interested in

FHA loans. Local insurance companies seemed to be fairly well loaned up and Mr. Deming anticipated it would be well into 1958 before this situation changed, but large outside companies had begun to be more active in this field. The brightest part of the picture in the Ninth District continued to be agriculture, Mr. Deming said, with the condition of livestock, the cattle feed situation, and the winter range situation all good. Most corn and soybeans were now out of the fields and there would be little loss from standing in fields over the winter. There was considerable wet corn which reduced its storage value and its price, and the lateness of the crop had slowed up cash income flow. Mr. Deming cited one other bright spot, noting that iron ore shipments this year were 7 million tons larger than last. One of the large mining farms was scheduling more developmental work this year than it did last year, pointing to another good year in 1958.

Mr. Deming said that he agreed it would be well to change the wording of the Committee's directive but would lean toward that suggested by Mr. Hayes, more than any of the other suggestions. He had no special target for net borrowed reserves but believed the level should tend down from that aimed at during the past three weeks, and he would leave to the Manager of the Account the determination of the precise level.

Mr. Allen said that retail trade in the Seventh District made a poorer showing in November than in the country as a whole.

For the week ending December 7, however, district stores were off 3 per cent, compared with 5 per cent for the nation. Automobile production schedules for December were reduced from 620,000 to 580,000. It was too early to talk about total production for 1958, Mr. Allen said, but a leading figure in the industry had expressed himself privately last week to the effect that sales for the year 1958 would not exceed 5.5 million cars. Despite poor sales currently, production was continuing at a good pace and the industry would not be surprised to show finished car inventories close to 800,000 units by January 1, and the feeling in Detroit was that this figure might rise to a million early in 1958. The reason for this expectation was usually expressed as fear of the labor negotiations which would take place in the spring and the possibilities of serious strikes at that time or before.

Mr. Allen reported on a meeting of business economists held at the Chicago Bank on December 11. The steel people then expected production in 1958 to total 109 million tons, 52 million in the first half of the year and 57 million in the second half. This would compare with an estimated total of 113 million tons in 1957. Appliance, radio, and TV people reported inventories to be in good shape with no evidence of panic selling or price slashing. Telephone company expenditures were expected to be about the same in 1958 as in 1957, both in Illinois and in the nation. Food sales were holding up well and food chains expected to add more stores in 1958 than in 1957. Agricultural machinery sales were expected to be as good in 1958 as in 1957 or slightly better. Housing expected a 10 per cent increase nationally in new starts.

Mr. Allen reported that the easier money conditions had shown up in reduced borrowings by Seventh District money market banks, but other district banks had shown increased borrowings with evidence that loan growth was continuing at the smaller banks. A survey of loans in the Seventh District in October brought out the disturbing factor that during July-October, more than 20 per cent of instalment loans on new automobiles had maturities of more than 30 months. In the same period of 1956, only six per cent of automobile sales were on contracts with maturities of more than 30 months.

Mr. Allen said that he would lean to a great deal that Mr. Irons had said about monetary policy. He would not like to see any notable easing in the next three weeks. Mr. Young had pointed out that despite the recessionary tendencies, business was still at a very high level. Mr. Allen thought he would not feel comfortable until there had been some reflection of adjustments in the retail price situation. The sooner this came, the better, and until then he would not favor conditions easier than those of the last few weeks. With respect to the Committee's directive, Mr. Allen said he was inclined to Mr. Hayes' suggestion. He would like to get back to a more general statement of policy rather than to try to be so specific in the directive.

Mr. Leedy said that the Tenth District level of employment was higher than a year ago, but there had been a recent reduction in employment both in manufacturing and in nonmanufacturing. Retail sales for the year to date were about the same as in 1956, but since October sales had been running behind last year. The one bright spot in the Tenth District was in agriculture, Mr. Leedy said. The weather recently had been favorable for harvesting the balance of the corn and Milo maize crops. It did not appear that earlier expectations of sizable losses of corn and maize because of wet weather would develop. The winter wheat crop was in excellent condition and making fine pasture. Prices of important agricultural products of the Tenth District were encouraging.

Banking statistics for the Tenth District continued contrary to the national picture. Loans had grown more since mid-1957 than in the previous year, particularly industrial and commercial loans. Cattle loans had been increased sharply at country banks because of favorable pastures and abundant feed.

Mr. Leedy turned to the availability of credit at the discount window, stating that in the Tenth District he would not wish to give any indication that the discount window was not open at this time.

Some bankers were more or less chronic borrowers, and efforts to correct that tendency might be intensified after the year end, but as a general proposition he did not think it appropriate to now apply general restraints to the use of the discount window. As to credit policy, Mr. Leedy said that the survey this morning confirmed that the country was in a recession. For the next three weeks he thought net borrowed reserves should trend downward with a benchmark of zero. After the first of the year, the Committee would be confronted with a softening of reserves, but Mr. Leedy did not wish any tightness to exist in the money market during the next few weeks. The Management of the Account should watch carefully the performance of the market and, to the extent that it could do so without setting off another round of increases in prices of Government securities, it should trend downward in net borrowed reserves. Mr. Leedy said that he felt that the wording of the directive should be changed and he would go along with general wording rather than trying to pinpoint the actions to be taken. Either the first half of Mr. Riefler's statement or the proposal Mr. Hayes had made would be suitable.

Mr. Leach said that reports of the past two weeks left no doubt that the downturn in the Fifth District economy, like that in the nation, was widespread and continuing, although it was still moderate. At the Richmond Bank's Directors' meeting last week, directors representing key industries in the district were all gloomy as to the short-term outlook.

With respect to the discount window, Mr. Leach said he thought both the law and the Board's regulation had established principles as to appropriate and inappropriate uses of this facility. These principles should not vary from month to month, and member banks must operate within those limitations, making such adjustments as become necessary. The System had several policy tools, Mr. Leach said, but the discount window was not one of these.

Present economic conditions make appropriate further moderation of reserve pressures, Mr. Leach said. This moderation should be gradual and the System should carefully avoid the creation of sloppy markets. More aggressive action than in recent weeks might well have caused an even more precipitate run-up in Government securities prices than had taken place. Mr. Leach said he believed the System was now in a position to bring about reserve availability more nearly in line with economic conditions and the discount rate action. Consequently, it would seem appropriate by the end of the next three weeks to attain conditions consistent with zero net borrowed reserves. However, in view of the uncertainty in the market consequent to the rapid run-up in prices and year-end strains, he thought that more than the customary emphasis should be placed on the feel of the market. As to the directive, Mr. Leach thought this a good time to change the wording. Either the proposal by Mr. Riefler or that by Mr. Hayes would be appropriate, although Mr. Leach leaned toward "mitigating recession" rather than "promoting recovery" at this time.

Mr. Mills said that the policy recommendations made by Mr. Hayes fitted rather closely his own policy reasoning. That would mean that reserves through the year-end would be supplied as freely as necessary comfortably to carry the money market and the banks over the year-end hurdle. After the end of the year, there was some question in his mind whether the Committee should have a conscious purpose in bringing negative free reserves down to the zero level. It could be preferable to take advantage as far as possible of the natural factors in the market that would tend to bring about that end and purpose.

Mr. Mills said he, too, had reservations about any magic residing in monetary policy as far as supplying reserves in quantity was concerned; that is, as to their efficacy in turning around the adversely shifting economic situation. His feeling would be that to free reserves in too great abundance would merely work toward rising market prices of U. S. Government securities and falling yields and would have the effect of stampeding commercial banks into a movement to extend their maturities which in turn would further aggravate the yield results on the down side at the same time that it tended to impair the liquidity of commercial banks at a time when their liquidity in the longer run might best be improved. That being the case, he would feel quite strongly that the Management of the Open Market Account should have complete discretion in regulating the supply of reserves and should be governed to a considerable degree by the feel of the market.

Mr. Mills doubted very much that banks would be inclined to expand their loans substantially at the present time or that they were apt to find the sort of demand, commencing with the new year, that would invite them to expand their loans materially. Mr. Mills said he shared the opinion regarding the operation of the discount window that had been expressed by Mr. Leach and others and believed that the Board's Regulation A allowed ample latitude to meet individual situations of member banks. He believed the discount window was not intended to be the primary agency for providing reserves and, as a device having only a secondary place in the reserve orbit, the general reserve treatment applied to member banks should be through open market operations or by timely adjustments in reserve requirements.

Mr. Robertson said that again he found himself pretty much in agreement with Messrs. Irons and Allen. It seemed to him that the plus and minus factors in the economy had been well set forth by Mr. Young. At the moment, he thought that the minuses had it and this was perhaps most dramatically shown by the declines in the index of industrial production and in Gross National Product, and by the increase in unemployment. However, Mr. Robertson thought there was great danger in overlooking the plus factors. We have to remember that we are still on a very high plane, he said. Wholesale prices still are very high, higher than a year ago, and show no signs of declining. Consumer prices are not only not declining but are showing positive signs of advancing. Consumer borrowing is not being reduced and is still increasing at the rate of increase prevailing over the past year. Demand for long-term funds is still high. Demand for houses continues strong--3 per cent above a year ago. Inventories are still high, though being reduced somewhat. In sum, Mr. Robertson was not impressed with the severity of the declines thus far, and he felt that it was necessary to add to these and other plus signs the prospect of deficit financing by the Government.

Mr. Robertson said that all of this led him to believe that the Committee might be magnifying an adjustment at a high level into a drastic recession. It would be unwise to flood the market with reserves, he said, and it was still necessary to have a firm hold on the reins in case this team which is now backing up a little should suddenly lurch forward. This did not mean we should maintain a tight position, but neither did it mean we should adopt an easy one. Mr. Robertson thought that an easy situation could start the upsurge of inflation all over again. We are in a different position than in the 30's, when "easy money" had little effect, he said, because the growth factors are much stronger than they were then. He thought the influence of easy money could be very effective today, as contrasted with the 30's, and that now we could "push on a string." Mr. Robertson also said that he thought that a lower volume of activity, such as we now have, called for a lower volume and velocity of money. His view would be to hold an even hand on credit policy and to be ready to move either way. This period more than many made it necessary to watch the situation very carefully because the Committee might have to move very fast. If activity were to go down, he would not object at all to easing, but he thought the Manager of the System Account was in better position than the Committee member to determine day-to-day needs, keeping in mind that the position he (Mr. Robertson) would like to see was an even keel as of the moment. Mr. Robertson also said he thought the Manager of the Account had done a good job of handling the account over the past two weeks. He would like to have no obvious change unless there was a change in conditions.

Mr. Robertson said he too thought the directive of the Committee should be changed. He leaned definitely toward Mr. Hayes' suggestion but would not be averse to a combination of that with Mr. Riefler's suggestion so as to have clause (b) of paragraph 1 call for operations with a view to "cushioning adjustments and to mitigating recessionary tendencies in the economy."

With respect to the discount window, Mr. Robertson said he agreed almost completely with the comments by Mr. Leach.

Mr. Shepardson said his story had been told three times this morning. He agreed completely with Messrs. Irons, Allen, and Robertson. There had been some downward trends but he thought the emphasis should be on the fact that we were still at a high level. We have been striving for some time for adjustments. We are in the process of getting some adjustments. Mr. Shepardson said he would go along with what had been said about maintaining restraint. He presumed of course that the System was going to provide needed reserves, but he felt it should keep a taut rein without a straining rein. So far as the Committee's directive was concerned, he leaned toward having clause (b) short and for not getting into shades of emphasis. He would take the first part of Mr. Riefler's suggestion under which clause (b) would be changed to call for operations that would "cushion adjustments in the economy."

Mr. Fulton commented that for some time he had been on the hard money side of the group. He noted that the steel, machine tool, and other basic industries which were of large importance in the Cleveland District had shown rapid deterioration within the past few weeks. It was surprising, he said, how this slowdown had become cumulative. There was more pessimism in the Cleveland District than had been reported for any other district so far this morning. There had been a prevalence of cutbacks in new orders and also in delivery schedules, which were being stretched out as needs of industry were being revamped. Steel mills of the district were all operating below 70 per cent of rated capacity. Coal production was down from a year ago. There were 13 areas in the district classed as "moderate" labor surplus areas, meaning that from 3 to 6 per cent of the labor supply was unemployed, and there were 11 areas classed as "substantial" labor surplus areas, meaning that more than 6 per cent of the labor supply was unemployed. Department store trade had been running below a year ago as had bank debits. Perhaps this was a classic recession brought on by an excessive capital goods boom and increased capacity which could not now be used, Mr. Fulton said. Many manufacturers believed that this downturn probably would be more severe and longer in duration than the 1953-1954 recession. In the auto industry, the guessing was that not more than 5.2 million passenger cars would be manufactured this year. In the next quarter there would be curtailment of production in the automotive field so as to avoid too unwieldy inventories for dealers. Bank loans had been declining largely as a result of inventory liquidation, but in the past week there had been a jump presumably because of tax borrowing.

Mr. Fulton said he felt the Committee should be moving toward zero free reserves, not dramatically or rapidly, but constantly. This would give relief that he felt was needed. The Cleveland Bank had been administering the discount window in accordance with the Board's regulation, Mr. Fulton said, and he felt this should not be a source of reserves except, as the regulation indicated, for an adjustment of the immediate needs of banks. He would like to see the Committee's directive changed and leaned strongly toward the wording suggested by Mr. Hayes or, as an alternative, the first phrase of the suggestion made by Mr. Riefler.

Mr. Williams said that the materials he had gathered for this meeting corroborated what Mr. Young had presented on the economic situation, and he would not repeat except to mention a few specific instances to sharpen the picture. Department store sales had slumped during the past two weeks but store officials were now expecting dollar volume for this year to total about the same as in 1956. Sentiment among seven business economists from whom information had been obtained on Third District business trends could be summarized as "murky weather and a falling barometer," Mr. Williams said. There was a general line of pessimism perhaps the most discouraging aspect of which was the decline in incoming orders. The gimmicks that had been tried for stimulating business had not succeeded. In general, no serious decline in total output was expected, although currently the business economists were quite pessimistic. This perhaps reflected an inability to see any stimulus that would lift output within the next few months.

After citing comments of a number of the individual business economists, Mr. Williams said that bankers expected some fall-off in loans but not too great a decline. Some large bankers had been paring their loans on a selective basis as a matter of policy. To some extent the reduction in outstanding bank loans since mid-summer of this year reflected the use of proceeds of new securities sales. Mr. Williams also mentioned a report of a moderate increase in demand for home loans, although it was expected that total loan demand would decline seasonally or possibly somewhat more than seasonally in the first part of 1958.

With respect to monetary policy, Mr. Williams said he felt that the bill rate should be around a 3 per cent rate structure. The reserve position of banks should not be eased enough to encourage any boom in the Government securities market, although reserves ought to be available. On the proposed rewording of the directive, Mr. Williams thought there was a little to be said in favor of the suggestion Mr. Hayes had made. The suggestion of Mr. Riefler incorporating the words "to promote recovery in the economy" would seem to call for positive action, and Mr. Williams felt that for the present the Committee should be playing by ear.

Mr. Bryan said that his only comment specifically on the Sixth District related to the severe freeze that had occurred since the preceding meeting, and which had caused great damage to vegetable crops and citrus groves in Florida. This would cause a reduction in Florida agricultural income, but Mr. Bryan thought that for the district as a whole it would not be a particularly severe factor. The over-all appraisal of the situation, he said, was that the Atlanta District was still operating at a high level, but the downward tilt in the district's economy was becoming, over all, more pronounced.

With respect to national policy, Mr. Bryan then made a statement substantially as follows:

> It appears that we are confronted with a problem of adjusting policy to an immediately current and deteriorating economic situation, at the same time facing the fact that the longer-run economic problem may still be one of an inflationary bias in the economy. The latter problem is complicated by a question to which we do not now, and probably cannot for a number of months, know the answer, namely, the impact of an almost certainly increased national defense outlay. The latter problem becomes very complex to my mind because we cannot now know the amount, manner of financing, or timing of the increased defense outlay.
>
> In this situation, it seems to me that our wisest course is to adapt policy to the currently available economic data. The greater danger, it seems to me, would lie in attempting to adjust monetary policy to elements of national policy that, at the moment, are indeterminate and hypothetical.
>
> Monetary policy, I believe, can play its most effective role in a downturn if monetary ease is injected during the early stages of a downward movement rather than after a recession is well under way and its effects are accumulative. On the basis of that thought, I am of the opinion that the System's policy has had, at best, a minimum adequacy to the developing situation.
>
> Thus far, the System has added to banking reserves in a modest amount over and above the seasonal drain. The

amount has been insufficient to affect even prime rates at commercial banks, let alone the general structure of bank rates. Among bank borrowers it has affected only the relatively few that have rates tied to the discount rate.

Thus rates in the capital markets have dropped substantially but more as a result, it seems to me, of seasonal factors, speculative activity, rumors, and expectations rather than as a result of System action to make funds actually more available. I suspect the price rally in the capital markets has been too rapid and insupportable for long, unless the System actually moves to increase the availability of bank reserves. I would regard a situation in which there were a capital market reversal, or ease simply by an accumulative weakening of the economic situation, to be dangerous at this time.

I attach great significance to the fact that, as of November 27, the private money supply (demand deposits and currency) was 0.4 per cent below its level a year ago. Total member bank reserves in November averaged 1.1 per cent below the average of November 1956.

What is happening, therefore, is that in the face of a now clearly perceptible economic downturn, our effective policy, whatever our intentions, has been to allow a reserve base providing for no growth whatever in the economy. I believe it clear that the continuation of such policy must finally be an important causative factor in promoting a serious recession.

Accordingly, I would advocate at this time the use of the Open Market instrument to provide for the remainder of December an amount of reserves clearly greater than those required by the year-end increase of loans and currency drain.

Mr. Bryan went on to say that the Committee's directive was clearly not appropriate to the present situation. He would favor the suggestion that Mr. Kiefler had made. In response to a question from Chairman Martin, Mr. Bryan said that he was not prepared to state a figure to be used as a benchmark for net borrowed reserves but that he certainly would tend downward towards zero.

Mr. Szymczak said that Mr. Bryan had delivered his speech. He thought the Committee would be back during the second quarter of next year doing the reverse of what it was now doing, but he favored what was now being done. As for the discount window, its use should be in accordance with the Board's Regulation A. As for the amount of reserves to be provided by the Open Market Account, he would provide reserves as permitted by the tone of the market, rates, and other factors in moving downward toward zero net borrowed reserves. As to the directive, he thought the wording suggested by Mr. Riefler more realistic than the others. He would accept the recommendation of Mr. Hayes because he thought it meant exactly what Mr. Riefler had proposed, but he thought Mr. Riefler's represented a more realistic approach.

Chairman Martin noted that this was the last meeting of the year 1957, and he said that he hoped the Committee would forgive him for taking this opportunity to make a few comments not specifically germane to what was at hand. Christmas time always made him cheerful, and perhaps anything cheerful that he said at this time should be discounted because it might be Christmas cheer.

In preparation for this meeting, Chairman Martin said that he had read the minutes of the meetings held during this period a year ago. He had tried to review his thinking at that period, and it was very easy to rationalize oneself into thinking that he had a position that he had not expressed at the time. However, he really was more optimistic at present than he was at this time a year ago. This did not mean that he did not think we were going to have a very difficult Congressional session, and there were many problems ahead for which the answers were not apparent. He recalled, however, that a year ago his thinking was along the line that there were so many chickens of inflation getting loose around the yard that it looked as though we would get into a hopeless situation and the chickens would all come back to roost at the same time. These chickens of inflation are coming home to roost now, the Chairman said, but he did not think they were coming back in a way that would make it completely hopeless to keep the henhouse in order.

Chairman Martin said that all of us would differ over the usefulness of money and credit policy. At the moment, he thought we were dealing in minor differences around the table. His own position was quite clear. He was on the side of moving towards zero free reserves. This seemed to him consistent and he believed that it would not create a sloppy money market. There was a recognition around the table of the problems of the Manager of the System Account and a general view that he should be given the maximum latitude in carrying on operations. The Chairman recalled his first Christmas with the Federal Reserve, when a very difficult period developed. That had not been a happy experience from his point of view, but he said that he learned a great deal at the time and he was convinced that the Manager of the System Account should be given all the latitude possible at this particular time of year.

The Chairman said that he differed with the suggestions that had been made that the Committee keep an even keel because he did not think we could keep an even keel at this time. The Committee either had to proceed in an orderly manner with its policy and trend in one direction, or it would not proceed at all to make its words and its policies meaningful.

Chairman Martin said he wished to say a word again about posture. In the early stages of this year, from the time the Federal budget got out of hand and it became clear that we were in an on-again-off-again budget and that inflation was getting ahead of us, the thing that had worried him most was that it appeared that the System was the only instrument of Government that was fighting inflation. This could be over-stated, but by July of this year the System had gradually assumed in the eyes of the public the position that it was the only agency fighting inflation. Despite the judgment that the System's efforts might not be very important in the whole picture, there could be a tendency to underestimate the forces of the System.

During the past summer, Chairman Martin said he was quite worried that the System might get into the role of being a crusader against inflation and that it would not be able to reverse its posture in time to make a general contribution to economic policy. Now, he thought that perhaps by an accident of the economy, the System's posture had been reversed in the nick of time. He thought that the diagnosis of an illness was important. He did not think that what the System was now doing was in the nature of giving a hypodermic but rather was more in the nature of a sedative. If he thought a hypodermic was needed, he would be in favor of a different approach from that we had taken.

He also questioned whether our situation was similar to that of 1953. He thought that the deficit financing that might be in the offing would not be an important factor at the moment. It might become so later, but for the moment any effects from that source were pretty minor. He noted that in order to make deficit financing effective it would be necessary to let contracts and to know where to spend the money if, when a downturn was on us, it was to have a major effect. It would take time to spend on such projects, and this was where economic planners got into difficulty: they would have ideas and they would have projects, but the timing gave difficulty. What he wanted to say at the moment was that it was very important for the System to have the right posture. It is true that we have been telling the public for a long time that just the situation we are now facing was bound to appear, and it is true that the System has encouraged some of the adjustments that are now occurring. Some of these adjustments had to come, and the Chairman thought they were coming and would come very quickly in the discount markets. He noted that there were quoted and unquoted prices and expressed the view that the price adjustments in the offing might become very dramatic.

A major concern was also with borrowed money, Chairman Martin said, because the likelihood of some scandal occurring was increased when borrowed money was involved. He did not refer to a scandal in dishonesty but he illustrated his thought by citing the building of a $200 million operation with $25,000 of capital and the weaknesses that were likely to result but which did not appear until the operation got into trouble. Without making a business forecast, the Chairman reiterated that it seemed to him that the posture of the System must be very clear at this time if it was to fulfill the role of wanting to minister to the patient in every way it could, of not contributing to unemployment, and of not taking the line that unemployment was desirable. It might be that unemployment was inevitable, the Chairman said, but the Federal Reserve should never lose sight of the fact that the man who is unemployed is in a special category. Here we come to the crucial problem of the "haves" and the "have nots." The man who has been out beating the bushes and who can not sell is in a different category from those who, for example, are in Government service. There was a crucial problem in this particular area and it involved noblesse oblige.

There were differences among the members of the Committee, the Chairman noted, and it was healthy to have such differences. Minority views should be encouraged at all times throughout the System although the System should try to develop a policy and to have that policy criticized and subjected to testing. He thought it very important that the Committee bear in mind, however, that there must be a positive, constructive approach on the part of the Federal Reserve System regardless of whether the public blamed it or criticized it. So far as diagnosing the patient, there were those chickens coming home to roost, Chairman Martin said. In his opinion, they were the chickens of inflation. It was too bad that the inflation got out of hand to the extent that it did. The Federal Reserve was not without blame, but it did the best it could with money and credit policy under all circumstances. At this time, however, Chairman Martin said he believed it terribly important that the posture of the System be one of sympathy and of wanting to help the patient. At the same time, it should not be a policy of softness.

Chairman Martin concluded his statement with the comment that it appeared that the Committee today came out with the majority taking the line, with which he agreed, that Mr. Hayes had presented. This would call for a change in clause (b) of the wording of the directive to be issued to the New York Bank which might be accomplished by a combination of the individual suggestions as proposed by Mr. Robertson, so as to have the clause call for "cushioning adjustments and mitigating recessionary tendencies." Chairman Martin said he thought the majority of the Committee to be in favor of a moderate reserve trend toward zero, although he recognized that minority dissents on the parts of Messrs. Allen, Irons, Robertson, and Shepardson had been indicated.

Mr. Shepardson said that to clarify his position, he had stated that he believed the Committee should hold a taut rein on the situation but he had also said he would change the wording of the directive to call for cushioning the adjustments that were taking place. This would imply that the Committee's operations would make some adjustments in the reserve position of banks.

Chairman Martin then inquired whether, in so far as the directive was concerned, there was any member of the Committee who would disagree with changing the wording of clause (b) of paragraph 1 of the directive to call for operations with a view, among other things, "to cushioning adjustments and mitigating recessionary tendencies in the economy." None of the members of the Committee indicated that they would dissent from the adoption of this wording.

Chairman Martin also inquired whether any of the members of the Committee would differ with the summary statement that he had made that a majority favored a moderate trending toward zero free reserves.

Mr. Shepardson said that he had suggested maintaining a taut rein, but he would not take exception to the statement to which Chairman Martin had just referred.

Mr. Irons said that he would indicate a mild dissent to trending toward zero free reserves.

Mr. Robertson said that the Chairman's summary covered his views.

Chairman Martin suggested that in the absence of other comments it would be understood that the directive with the revised wording agreed upon would be approved and the summary that he had given of the views of the Committee would be accepted.

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 cushioning adjustments and mitigating recessionary tendencies in the economy, 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 a draft of letter to Congressman Abraham J. Multer that had been prepared in accordance with the discussion at the meeting on December 3 of Mr. Multer's request of November 22, 1957, for information on operations of dealers in Government securities. He noted that the draft reply had been circulated to the members of the Committee, and he inquired whether there were any suggestions for change.

Mr. Hayes said he had no suggestions for change in the letter. He added, however, that the answer to Congressman Multer raised a question in his mind as to whether the Committee was getting all the information from dealers in Government securities that it needed for its own purposes, and he suggested that consideration might be given to this question by the Special Committee.

Mr. Allen said that he had no suggestion for change in the letter. He inquired, however, whether the information Congressman Multer was requesting had been disclosed to representatives of Congressman Patman when they visited the New York Bank recently.

Mr. Rouse stated that he was not at the Bank at the time Mr. Patman's representatives made their visit but that it was his understanding that the information was not disclosed to them. They were aware before coming to the Bank that Government securities dealers furnished this type of information to the New York Bank.

Mr. Leedy raised a question as to the sentence in the draft letter that indicated Congressman Multer might request individual dealers in Government securities to furnish information that might assist him in his inquiry and, after discussion as to whether such a suggestion should be made, it was agreed that the sentence in slightly revised form should be included.

Thereupon, a letter to Congressman Abraham J. Multer prepared for Chairman Martin's signature was approved unanimously in the following form:

Your letter of November 22, 1957 was taken up at the latest meeting of the Federal Open Market Committee. It was the view of the Committee that, inasmuch as the daily reports of dealers' operations in U. S. Government securities are furnished by the dealers on a purely voluntary basis and in the strictest confidence, it would not be within the discretion of the Federal Open Market Committee or the Federal Reserve Bank of New York to disclose information received in connection with these reports.

Should you wish to do so, you could of course direct your request to the individual dealers in Government securities.

Mr. Robertson referred to the System Committee for the Study of Float appointed pursuant to the discussion at the meeting of the Federal

Open Market Committee on August 7, 1956 (Messrs. Erickson, Johns, and Robertson, Chairman). At the Open Market meeting on May 7, 1957, he (Mr. Robertson) had reported that the Committee on Float had received a document from its subcommittee and that it expected to distribute copies of its report shortly. Subsequently, the report of the System Committee for the Study of Float dated May 31, 1957 was submitted, and that report was considered by the Conference of Presidents of the Federal Reserve Banks on June 17, 1957. Mr. Robertson went on to say that the System Committee for the Study of Float also had prepared a report dated December 16, 1957, addressed to "The Members of the Board of Governors and the Presidents of all Federal Reserve Banks." The report had been addressed in that fashion because it referred in part to policy matters for consideration by the Federal Open Market Committee and in part to operating matters pertaining to check collection as such without reference to the impact of float on open market operations. Mr. Robertson said that the Committee recommended:

1. That the Open Market Committee determine certain policy questions listed in the report and give the Management of the Open Market Account appropriate directives as to the approach it should take with respect to float; and

2. That the other studies referred to in the program submitted with the Committee's report of May 31, 1957, be made under the direction of the appropriate committees of the Presidents' Conference.

After stating that the December 16, 1957 report of the System Committee for the Study of Float would be distributed by the Secretary of the Open Market Committee in the usual manner, Mr. Robertson said that in a separate report dated November 14, 1957, the Subcommittee on Float recommended a change in the information telegraphed daily by the individual Federal Reserve Banks to the Federal Reserve Bank of New York to provide the Open Market Account Management with data on float, reserves, and borrowings. A draft letter embodying such recommendations, which letter would supersede the letter from the Board of Governors to the Federal Reserve Banks dated August 7, 1957, was distributed at this point, and Mr. Robertson said that the Committee for the Study of Float recommended that the Board send the proposed letter promptly, requesting that the revised procedure for reporting figures be put into effect, if practicable, beginning with the figures for Thursday, December 26, 1957. He went on to say that the proposal for reporting data was still experimental although it had been cleared with a number of the Federal Reserve Banks and that it could be changed at any time that a change seemed desirable.

Mr. Mills inquired whether there was any risk that the operating officers of the Federal Reserve Banks might feel that they were having forced on them without previous review a revision in the procedure for reporting the data concerned, and in response several of the Reserve Bank Presidents indicated that they did not see any objection to sending out the letter in the proposed form.

Mr. Bryan stated that if the letter was sent out his Bank would, of course, do its best to furnish the information as requested.

However, he wished to say that he was opposed to this whole approach. He felt this a typical System mechanism by which we take up little problems while avoiding fundamental problems. The fundamental problem here was the degree to which the Open Market Account should attempt to adjust its operations to changes in float and similar influences. This was a problem on which the Committee had not come to a decision.

Mr. Robertson said that the Committee for the Study of Float hoped that the recommendations in its report, which was being distributed by the Secretary, would result in having the Federal Open Market Committee come to grips with this problem at an early date.

Chairman Martin suggested that the Committee approve the sending by the Board of Governors of the proposed letter, with the understanding that the Federal Reserve Banks would start furnishing the information in the new form beginning with figures for Thursday, December 26, 1957, if practicable, and in any event not later than January 9, 1958.

This suggestion was approved unanimously.

> Secretary's Note: The letter was sent later in the day by the Board of Governors to the Presidents of all Federal Reserve Banks except New York, with a copy to New York. A copy has been placed in the files of the Federal Open Market Committee.

It was agreed that the next meeting of the Committee would be scheduled for 10:00 a.m. on Tuesday, January 7, 1958.

Chairman Martin referred to the proceedings of the Tribunal set up by Parliament to inquire into the alleged leakage of information about the September 19 increase from 5 to 7 per cent in Bank rate of the Bank of England. He noted that the proceedings, which commenced at the Church House, Westminster, London, on Monday, December 2, 1957, were being reported in detail in The Times and suggested that they would be of interest to many persons within the Federal Reserve System because of the problem that was raised of possible conflicts of interest. The Chairman also said that the proceedings before the three-man Tribunal should impress all of those attending the Open Market meetings with the necessity for keeping matters discussed at these meetings completely confidential.

Thereupon the meeting adjourned.

Secretary's Note: Chairman Martin then referred to a wire which he had sent to the Chairmen of all Federal Reserve Banks on December 10, 1957, concerning a draft letter which the Secretary of the Treasury planned to send to the Small Business Administration regarding financial problems of small business, and there followed a discussion of the views that had been expressed by a number of the Reserve Banks in reply to the inquiry.

Winfield W. Riefler
Secretary