



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

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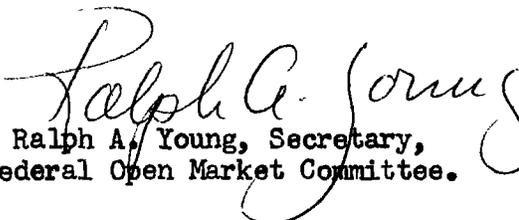
CONFIDENTIAL (FR)

TO: Members and Alternate Members of the Federal
Open Market Committee, other Reserve Bank
Presidents, and Messrs. Thomas and Rouse

FROM: Mr. Young

There is enclosed a copy of a memorandum dated March 7, 1960, reflecting in some detail the discussion of continuing operating policies and the form of the directive during the latter part of the meeting of the Federal Open Market Committee on March 1, 1960. This is not being distributed as a part of the minutes for approval, but if you have any comments or suggestions regarding the memorandum they may be sent to me.

Very truly yours,


Ralph A. Young, Secretary,
Federal Open Market Committee.

Enclosure

CONFIDENTIAL (FR)

RECORDS SECTION

Committee discussion (Executive Session) on March 7, 1960, concerning the Committee's statement of continuing operating policies and also the wording of its current directive to the Manager of the Account.
(Based on Secretary's rough notes and recollection)

March 7, 1960.

PRESENT: Mr. Martin, Chairman
Mr. Hayes, Vice Chairman
Mr. Balderston
Mr. Bopp
Mr. Bryan
Mr. Fulton
Mr. King
Mr. Leedy
Mr. Mills
Mr. Robertson
Mr. Shepardson
Mr. Szymczak

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

Messrs. Erickson, Johns, and Deming, Presi-
dents of the Federal Reserve Banks of
Boston, St. Louis, and Minneapolis,
respectively

Mr. Young, Secretary
Mr. Thomas, Economist
Mr. Rouse, Manager, System Open Market
Account

In opening the discussion, Chairman Martin expressed concern regarding the evident division of opinion within the Committee regarding the desirability of the present form of the Committee's statement of continuing operating policies, the frequently expressed outside views as to the rigidity of these policies, and the problem the policies have recently presented in meeting a seemingly reasonable request of the Treasury. He stated that it was natural enough to have doubts and questions arise after seven or eight years. It was possible that the Committee had not been as flexible as it might have been in adapting its policies to different situations, both from its own standpoint and from the standpoint of the observer on the outside. However that might be, it was important to have on the table such differences of opinion as there were within the Committee and such outside criticisms as had been expressed, so that each member was familiar with all of the issues. It was with this thought of

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full information on the issues that he had asked the Committee's secretary to circulate a documentation that included: (a) pertinent extracts from past minutes relating to the continuing statement of operating policies; (b) such suggestions for changes in the statement as had been advanced by different Committee members and staff; (c) a specific defense of "bills only" prepared by the Treasury staff for the Secretary's use; and (d) an inventory of issues of continuing operating procedures prepared by the secretary. While there were differences of viewpoint within the Committee, he regretted very much that the differences had been advertised outside the Committee as a New York Bank-Board split.

Mr. Hayes then commented that he regretted any outside misunderstandings as to the state of mind within the Committee but felt in general that such misunderstandings had been kept to a minimum. So far as his own thinking about the problem went, he did have the feeling that the Committee's operating policies had come to be viewed on the outside as unduly rigid and doctrinaire. He himself deplored this very much and it had been his hope, and he had urged from time to time, that the statement of these operating procedures or policies might be modified so that it would be read on the outside as less doctrinaire and rigid than the policies were being judged. He thought the suggested draft revision of the statement of operating policies, recently prepared by the staff (Rouse-Thomas-Young) Committee, had gone a long way in meeting his ideas and he hoped that other members of the Committee would regard these suggestions as favorably as he did.

Concerning the question raised by the Treasury regarding System help in the refinancing of the April bills and the 2-1/2's of 1961, Mr. Hayes felt that the Committee had a responsibility for examining the issues on their merits. He himself believed that the System ought to do what it could to help the Treasury when that did not interfere with the System's own responsibilities. In any case, the Committee now faced this question since it had been raised by the Treasury and the Committee was obliged to respond favorably or unfavorably with its reasons. He suggested that the Committee's consideration of the matter might be furthered by asking the same staff committee to study the already prepared staff memos on the financings in question and to make recommendations to the Committee as to possible System help in them. He felt that any action that the Committee took in these two cases might go some distance in resolving certain of the underlying issues concerning the Committee's operating policies.

At this point Mr. Allen interjected comment to the effect that the Committee's problem as to its statement of operating policies might be alleviated, if not resolved, by combining this statement with the Committee's directive to the Manager of the Account, thus obliging the Committee to review the statement of operating policies every three weeks when it issued a new directive to the Manager. One of the problems for the Committee inherent in a statement adopted at the beginning of a Committee year was that the Committee was binding itself for the full year.

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Mr. Hayes then continued his comment with further observation that up to this point he had gone along with clause (a) of the continuing statement of policies with its reliance on the word "solely," but that he now felt that the word "solely" was too limiting. Another legitimate objective for the Committee's operations would be that of assisting the Treasury in effectuating its financings.

Governor Szymczak next addressed himself to the history of the Committee's operating procedures in the light of his experience as a member of the Committee. He recalled how, before the War, the Committee had committed itself to the objective of maintaining an orderly market for Government securities and how this commitment, once the nation got involved in war financing, led directly into the pegging of Government securities prices. In the light of his extended contact with the Committee's operations, he would question the wisdom of any change in the Committee's operating policies with a view to helping the Treasury in effectuating its financing, not that such a change in itself would be so dangerous but that no member of the Committee would know, if the Committee set out on such a line, just how far it would have to go in giving assistance to the Treasury and whether in the process of giving such assistance it would become dominated by the Treasury. What would be the reaction of the dealers, he asked, if the Committee were to make a change now in the wording of its operating policies from "solely" to "primarily"? What might happen by way of general market reaction to any such change? There would be many problems ahead.

While he personally did prefer the word "primarily" rather than the word "solely" in clause (a) of the statement, he doubted whether such a change would be advisable. Certainly, it would be only practicable if there were some obligatory rule as to make exceptions to the general rule because exceptions would occur typically at the prompting of the Treasury. Treasuries all over the world are under constant pressure to make use of the central bank to resolve their own problems.

Mr. Erickson was obliged to withdraw from the meeting at this point, so the Chairman asked him if he didn't have some commentary to make before he left. Mr. Erickson replied that as a first step for the Committee's consideration of its continuing operating policies he would like to see recommendations by the staff committee concerning suggestions for System underwriting help in connection with the April bill refunding and subsequent refinancing of the 2-1/2's of 1961. He also stated that of all the papers containing suggestions for the reformulation of the Committee's statement of operating policies, he liked the one prepared by Mr. Thomas the best, primarily because it stated the purposes in positive terms rather than as actions to be avoided.

Mr. Leach questioned whether the Committee was ready to make a choice as between using the word "solely" or the word "primarily." He felt that there ought to be a full exploration of possible exceptions that might

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occur if the Committee used the word "primarily." Also, he thought it might be better to provide explicitly for such exceptions.

Governor Robertson felt that the Committee had definite need for a continuing statement of operating policies. Public criticism of the statement, of which there had been a great deal, focused primarily on the confinement of transactions to short-term securities--in other words, to "bills only." He thought we could introduce a sense of flexibility in the statement's wording here if, for this rather negative formulation, we substituted a positive wording that directed the Manager to transact his business for the Account in that sector of the market that would entail the least interference with the economic functioning of the market.

Mr. Hayes thought that a reformulation along this line might not be entirely successful. There were risks, he said, that the Committee would narrow and make more rigid its formulation rather than introduce flexibility.

Mr. Bopp observed that our present use of the word "solely" was not appropriate because the Committee was not, in fact, operating "solely" for purposes of monetary policy when it followed an "even keel" approach during Treasury financings.

Mr. Johns questioned the "least interference" formulation suggested by Governor Robertson, doubting indeed whether any change along such lines could be made that would not disturb the market. People, he said, were going to study the statement closely for any changes and read into these changes modifications on the part of the Committee which the Committee might not have at all.

Governor Szymczak concurred with the thought that any change in the statement at this time was risky.

Mr. Johns stated that he had never himself considered the present statement of continuing operating policies as formulated to be rigid or doctrinaire. The Committee, he said, could not be bound for all future time by the statement and, in fact, the Committee had deviated from the statement from time to time as circumstances had warranted. He contended that the charge of rigidity in the statement was a charge brought solely by those who opposed the principles which the statement expressed.

Mr. Hayes, on the other hand, thought there was a real tendency for the Committee's present statement to be an inhibiting force in Committee decisions. He himself would doubt whether modification of the statement would cause the Committee to go to extremes.

Governor Szymczak noted that the question was not one of getting involved in pegging but rather of getting involved in continuing support of Treasury financings.

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Governor Mills next offered as his thinking that the Committee has been too obdurate. While he agreed with Mr. Johns as to the essential flexibility of its wording, the Committee's treatment of the wording, he felt, had been somewhat on the rigid side. He would favor experimentation in key wording, and so would incline towards shifting to "primarily" from "solely."

Mr. Mangels stated that the preceding round-table discussion impressed on him the desirability of dropping the continuing statement of operating policies as a once-a-year item and consolidating the substance thereof with the directive, making the consolidated item subject to review every three weeks. He suggested that the Manager of the Account and the Secretary of the Committee, following each meeting, compose for the record a written interpretation of the Committee consensus and the directive. This, he argued, would help clarify the record.

Governor King expressed himself as favoring the kind of policy statement that we have. He would substitute the word "primarily" for the word "solely," however. He thought that the extension of some kind of underwriting accommodation to the Treasury was a special question which might be compartmentalized, at least for the time being. He noted that the Federal Reserve was under sharp criticism in part for political reasons and in part for sincerely held views and convictions. He strongly felt that the situation called for adherence to a posture of open-mindedness.

Mr. Bopp expressed the hope that the Committee would give some thought to the possible desirability of shifting some part of its transactions in times of recession from the short- to the long-term sector of the market. He emphasized this might have helped in the 1958 recession experience, but agreed that the suggestion was a highly moot one and one that would need much study and critical thought before the Committee embraced it.

Chairman Martin then expressed himself as feeling that the whole review had been very helpful and that it had clarified for everyone the shades of difference of feeling about the continuing statement of policies. There was clearly a consensus favorable to reviewing the matter, but it was also evident from the discussion that it would require very careful thought and full discussion before any change was made. The Committee was in a sense the victim of history, but this history and record was a very important part of the story, and everyone needed to pay due regard to it. He, therefore, interpreted the consensus (without dissent) to be that the existing statement of operating policies be continued on a temporary basis and the matter of the substance be brought up again for discussion after individual members had had an opportunity to develop their respective thinking further.

With regard to the suggestions that the Committee might provide some advance help to two forthcoming refinancings, he referred the already

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prepared staff memoranda on the subject (one by Mr. Keir of the Board's staff and one by the Securities Department of the New York Bank) to the staff committee, consisting of Messrs. Rouse, Thomas, and Young, for further study and recommendation to the next meeting of the Committee.

Concerning a directive to the Account for this meeting, a motion was made and carried without dissent that clause (b) of the directive be modified to read:

"to fostering sustainable growth in economic activity and employment while guarding against excessive credit expansion."