

Minutes of actions taken by the Board of Governors of the Federal Reserve System on Friday, February 8, 1957. The Board met in the Board Room at 10:00 a.m.

PRESENT: Mr. Balderston, Vice Chairman
 Mr. Szymczak
 Mr. Vardaman
 Mr. Mills
 Mr. Robertson
 Mr. Shepardson

Mr. Sherman, Assistant Secretary
 Mr. Fauver, Assistant Secretary
 Mr. Thomas, Economic Adviser to the Board
 Mr. Vest, General Counsel
 Mr. Leonard, Director, Division of Bank Operations
 Mr. Young, Director, Division of Research and Statistics
 Mr. Sloan, Director, Division of Examinations
 Mr. Dembitz, Assistant Director, Division of Research and Statistics

There were presented telegrams to the following Federal Reserve Banks approving the establishment without change on the dates indicated of the rates of discount and purchase in their existing schedules:

Richmond	February 6
St. Louis	February 6
San Francisco	February 6
New York	February 7
Philadelphia	February 7
Cleveland	February 7
Atlanta	February 7
Chicago	February 7
Minneapolis	February 7
Kansas City	February 7
Dallas	February 7

Approved unanimously.

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The Board then considered a memorandum dated February 6, 1957, from Messrs. Young and Vest, which had been distributed prior to the meeting, relating to a request for a report on S. 719, to provide for national investment companies under the supervision of the Board and with funds provided by the Federal Reserve Banks, and on S. 720, to provide for insurance of loans to small business. Mr. Vest pointed out that these bills were virtually identical with bills introduced in the Congress in 1955, except that in 1955 it was provided that the Board of Governors would be the insuring agency in insuring lenders on loans to small business, whereas it was now proposed in S. 720 that the Small Business Administrator would do the insuring.

There followed a general discussion of the draft letter to Senator Fulbright during which numerous suggestions for reorganization and revision of the contents were made.

Following the discussion, Governor Balderston suggested that Messrs. Vest, Riefler, Young, and Thomas rework the draft and that a revised draft be submitted for the consideration of the Board.

There was unanimous agreement with Governor Balderston's suggestion.

During the preceding discussion, Messrs. Riefler, Assistant to the Chairman, and Allen, Economist, Business Conditions Section, Division of Research and Statistics, entered the meeting.

The Board turned to the memorandum of Governor Shepardson dated February 6, 1957, which had been distributed prior to the meeting, relating to farm credit problems in the drought area. Governor Shepardson

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explained that the report and the suggested letter to Secretary Benson grew out of his participation in the January 14-16 meeting on drought problems held at Wichita, Kansas, in connection with the President's visit there. There was a question, he said, whether the Board as a whole would want to take a position on this matter or whether the letter should merely reflect his individual views. He indicated he would like to see the letter go forward as a Board position if that was agreeable. The position taken in the letter, he felt, would provide support for the Secretary of Agriculture in holding a reasonable line on the use of additional credit in meeting the existing problem.

A discussion of the contents followed, during which a suggestion for rewording one sentence was offered. Governor Vardaman suggested that the letter go forward as a Board position over Governor Shepardson's signature.

There was unanimous agreement with Governor Vardaman's suggestion.

Secretary's Note: The letter, which was sent to Secretary Benson over Governor Shepardson's signature later in the day, read as follows:

With respect to the recommendations on credit problems that were drawn up at the special meeting in Wichita on January 14-16, I am authorized to make the following comments on behalf of the Board of Governors of the Federal Reserve System.

While this meeting was called to consider problems of drought and other natural disasters, primary attention seemed

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to focus on the drought problem. In this connection, it seems important to point out the significant differences between drought disasters and those resulting from fire, tornado, or earthquake. Disasters of the latter type are usually unforeseeable, infrequent, of short duration, and measurable in their effect. Drought, on the other hand, especially in the Great Plains area, is a natural hazard of the area. It is a constant menace, recurring frequently with varying degrees of duration and intensity. The severity of its effects is extremely difficult to measure and is to no small degree dependent on the type and method of operation and the prudence of the operator in providing adequate reserves.

It is axiomatic in any business that the projections of potential returns as a basis for extension of credit must take into account the risks involved.

Without commenting on the need or justification for drought relief measures or on the type of land-use principles that should be followed, it is assumed that credit decisions will be predicated on the development of the soundest possible land-use program and on such steps as may be feasible to help farmers accumulate proper reserves against future emergencies and to develop insurance programs to mitigate the economic effects of losses caused by natural forces in the future. In this connection, it seems clear that wider use of crop insurance or similar protection has great long-range potentialities for putting farm credit on a sounder basis, and the Board will be interested in further developments in this field.

The Board wishes especially to express agreement with the following comments of the Wichita report on the relationship between credit and income:

"The major economic problems in the drought area arise from lack of income. If credit is substituted for income over long periods, it builds debts which are beyond the ability of farmers and ranchers to repay, even under favorable weather conditions . . . Emergency loan programs should not operate to encourage borrowers to continue submarginal operations to their own ultimate detriment."

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The Board sees no reason why the period within which the Farmers Home Administration can make special livestock loans should not be extended for a further 5-year period, as the report suggests.

The Board is also sympathetic with the idea of permitting the Farmers Home Administration to extend livestock loans on an amortized basis adjusted to income with maturities longer than the present 3-year limit, although the question whether the maximum period of amortization should be as long as 10 years would seem to call for further study.

It does not appear desirable for the interest rate on loans of this kind to be reduced further below the rates prevailing at private or cooperative lending agencies in the affected areas. This matter is related to the question of encouraging private lenders to go further in expanding their farm lending activities and in adapting their practices to the needs of farm borrowers. FHA terms should not be made so favorable that farmers who might be able to borrow from private or cooperative sources would turn to the FHA. Only borrowers who cannot secure credit elsewhere "on reasonable terms" are eligible for FHA loans, but FHA interest rates should not be so attractive as to give farmers an incentive to try to prove that they are not regarded as credit-worthy by private or cooperative lenders.

It is true that there are certain fields in which the Government now makes loans at low special interest rates, but it would seem preferable to avoid any further spread of this device. Such help as is needed in the drought area -- whether for farmers or for businessmen -- should take other forms rather than subsidized interest rates. Otherwise, the redevelopment of the private credit system so that it will function effectively in these areas will be handicapped.

The Wichita report also suggests that the Farmers Home Administration be empowered, in connection with special livestock loans, to refinance existing debts and to pay the annual instalments on real estate loans. The Board doubts whether these changes are necessary. In any case, if refinancing is authorized, it is assumed that the FHA would not ordinarily refinance the full amount of an existing debt; for example, where the existing debt is a cattle loan, sound practice would require that the refinancing be on the basis of current appraisal values.

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While the recommendations on FHA relate primarily to livestock loans, it is assumed that any principles adopted in this field would also be applied where appropriate to other kinds of farming operations.

With respect to the recommendations on Small Business Administration loan procedures and standards, the Board considers that these could appropriately be given consideration by that agency. As to the proposal for SBA help in the development of new industries in the drought area, regardless of the size of the industry, this would seem to involve a complex set of considerations, and the Board would have serious doubts whether this approach would be appropriate or effective.

It is hoped that the foregoing comments will be of help in your consideration of these financial problems, and the Board will be pleased to discuss further any aspects that you consider desirable.

Governor Vardaman then suggested that arrangements be made for each member of the Board to have an opportunity to read a recent speech by the Majority Leader of the Senate, Senator Lyndon Johnson, in which he reviewed credit conditions with particular emphasis on the maldistribution of the available supply of credit. He pointed out that the speech was especially appropriate in the light of the morning's discussion.

The meeting then adjourned.

Secretary's Note: Governor Shepardson today approved on behalf of the Board the following items:

Memoranda from appropriate individuals recommending transfers of the following persons on the Board's staff, with increases in basic annual salaries, as indicated, effective February 10, 1957:

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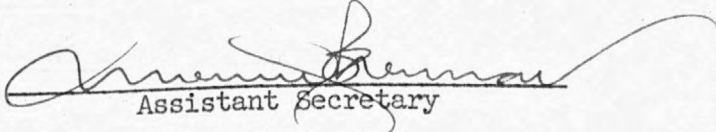
<u>Name and title</u>	<u>Basic annual salary</u>	
	<u>From</u>	<u>To</u>
Ruth Elizabeth Morris, from Secretary to Mr. Thurston, Assistant to the Chairman, to Secretary to Governor Szymczak	\$5,375	\$6,390
Nancy B. Kelly, from Secretary in the Division of Research and Statistics to Secretary to Mr. Thurston, Assistant to the Chairman	\$4,350	\$4,970

Letter to Mr. Armistead, Vice President, Federal Reserve Bank of Richmond, reading as follows:

In accordance with the request contained in your letter of February 5, 1957, the Board approves the designation of the following employees of your bank as special assistant examiners for the Federal Reserve Bank of Richmond for the purpose of participating in the examination of State member banks only:

C. Wesley Barker, Jr.
 Everett G. Melton
 Clarence E. Proffitt
 Johnson N. Snoddy, Jr.

The Board also approves the designation of James R. T. Hodgson as a special assistant examiner for the Federal Reserve Bank of Richmond for the purpose of participating in the examination of State member banks only, except The Bank of Virginia, Richmond, Virginia.


 Assistant Secretary