Minutes for June 6, 1957

To: Members of the Board

From: Office of the Secretary

Attached is a copy of the minutes of the Board of Governors of the Federal Reserve System on the above date.

It is not proposed to include a statement with respect to any of the entries in this set of minutes in the record of policy actions required to be maintained pursuant to section 10 of the Federal Reserve Act.

Should you have any question with regard to the minutes, it will be appreciated if you will advise the Secretary's Office. Otherwise, if you were present at the meeting, please initial in column A below to indicate that you approve the minutes. If you were not present, please initial in column B below to indicate that you have seen the minutes.

	A	B
Chm. Martin		x WM
Gov. Szymczak	x MSS	
Gov. Vardaman	x	
Gov. Mills	x	
Gov. Robertson	x R	
Gov. Balderston	x CCB	
Gov. Shepardson	x CCS	

Minutes of actions taken by the Board of Governors of the Federal Reserve System on Thursday, June 6, 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. Kenyon, Assistant Secretary
Mr. Thurston, Assistant to the Board
Mr. Thomas, Economic Adviser to the Board
Mr. Young, Director, Division of Research and Statistics
Mr. Sloan, Director, Division of Examinations
Mr. Hackley, General Counsel
Mr. Cherry, Legislative Counsel
Mr. Molony, Special Assistant to the Board
Mr. Noyes, Adviser, Division of Research and Statistics
Mr. Koch, Assistant Director, Division of Research and Statistics
Mr. Hexter, Assistant General Counsel

Report on bills to amend the Small Business Act of 1953. Copies of a revised draft of letter to the Chairman of the Senate Banking and Currency Committee reflecting the comments made at yesterday's meeting had been sent to the members of the Board.

Certain suggestions for further changes were made, following which unanimous agreement was expressed with the form of the letter.

Testimony on S. 2160. Pursuant to the understanding at the meeting yesterday, there had been sent to the members of the Board copies of a preliminary draft of testimony to be given by Vice Chairman Balderston next Tuesday, June 11, before the Subcommittee on Small Business of the

Senate Banking and Currency Committee concerning S. 2160, a bill cited as the National Investment Company Act of 1957. This bill, introduced by Senator Sparkman for himself and others, constituted a revision of the Fulbright bill (S.719) concerning which the Board reported by letter earlier this year to the Senate Banking and Currency Committee.

Mr. Young said that the staff had endeavored to present in this draft the kind of testimony that would be consistent with the thinking most recently expressed by the Board on the problem of financial assistance to small business and that it was in harmony with what the staff understood to be the views of Chairman Martin. One of the basic questions involved was whether the Board would want to go along with the proposal for establishment of national investment companies and, if so, what position the Board wished to take with regard to the capitalization of such companies and their supervision.

The first comments concerning the draft of testimony were made by Governor Robertson, who addressed himself principally to the portions of the draft concerning commercial bank participation in State development corporations. In essence, it was Governor Robertson's view that the draft went too far in the direction of suggesting more extensive participation by commercial banks in the activities of such corporations. With regard to the question of Federal Reserve or other public participation in new financing institutions designed to provide longer-term debt or equity financing for small businesses, he felt that a clear line of distinction should be drawn between the use of Federal Reserve funds ("high-powered dollars") and appropriated Government funds. In his opinion, the testimony should take the firm position that if the Congress found a need for the Government to provide funds for such institutions, this should be done through the use of appropriated money and with specific provisions included which would take the Government out of the lending business as soon as practicable.

Governor Mills said that he agreed completely with Governor Robertson's comments, as did Governor Vardaman. The latter also suggested making it clear in the testimony that, for the most part, the longer-term financing apparently needed by small businesses could not properly be extended by commercial banks.

Governor Shepardson then said it was important to recognize that there had grown up, whether with adequate justification or not, a rather strong body of opinion that a need existed for some additional mechanism to supply small business financing, and that apparently some legislative action would be taken in this area. After noting the relationship of any such activity to the effectiveness of Federal Reserve credit policy, he said that if an agency were set up to extend this type of credit, it seemed inevitable that the agency in the course of time would tend to expand its operations. Therefore, although he was not prepared to advocate such a program, it seemed to him preferable that any such activity, if approved by the Congress, fall under the supervision of the Federal Reserve System rather than some other agency over which the Federal Reserve would have no control. With respect to Governor Robertson's comments about the use of high-powered Federal Reserve dollars, he said that under any circumstances the Federal Reserve System was going to make available a certain amount of credit to meet the needs of the economy and, if the Congress should decide on and delegate to the System a small business financing program whereby a certain amount of credit would be channeled to that particular segment of the economy, the Federal Reserve could consider the extent of that activity in determining its over-all credit policy. However, reconciliation of objections might be more difficult if the Congress authorized such a program and established it outside the control of the Federal Reserve System. Therefore, even though the Board might question the desirability of such a program, he doubted whether the Board should take the position that it did not want anything to do with it. If the Board had supervision over the program and exercised discretion in keeping it within the over-all requirements of the economy, it appeared to him that in this way the Federal Reserve System could do far more to maintain its position and to assure the continuation of an effective monetary and credit policy.

Governor Balderston stated that in his thinking on the matter he had started with several assumptions, the first being that not too much was known about the institutional gaps in the field of small business financing or how those gaps might best be filled. It appeared that the answers could be obtained only by a much more definitive study than had been made to date, and it seemed to him that it would be advisable for the Federal Reserve System to undertake such a study on its own initiative rather than to have the study ordered by other parties. Pending the completion of such a study, it seemed likely that something could be learned by experimental operations. For example, from the experience of the State development corporations, it appeared that the real control and drive must be local rather than national. Turning to a related point, he suggested that in a matter of this kind the Federal Reserve System had become rather vulnerable by reason of the capital and surplus of the Federal Reserve Banks that had been built up, since it was tempting to suggest that this could easily be a source of funds for some program such as the financing of small business. While the Board should not be influenced by this appearance of vulnerability in its judgment as to what was best for the country, it should recognize that strong pressures were being exerted at the Congressional level to institute some kind of a program for the extension of credit to small business, and perhaps the best role that the Board could play would be one of endeavoring to influence the Congress in favor of the best choice among a number of alternatives. To summarize, he felt that a study was needed, that the study should be conducted by the Federal Reserve System on its own initiative, that interim experimental work would be desirable, that perhaps the initiative in supplying the experimental funds should be taken by the System, and that the furnishing of any such funds should be accompanied by a certain amount of over-all supervision.

Governor Balderston went on to say that he had a great deal of sympathy with the traditional approach of the Board to this kind of problem, especially on the point that the Federal Reserve ought not become involved in the allocation of the total amount of available credit. However, he was concerned, as he had said, that the capital and surplus of the Federal Reserve Banks had come to represent an inviting target, expecially with the current pressure on the Congress to do something to provide financial relief to small business. His thinking differed somewhat from that of Governor Robertson in respect to the use of Federal Reserve dollars, not from the theoretical standpoint but because the capital funds involved in the small business financing program would be relatively small and he wondered whether an argument based on the inflationary effect of the use of Federal Reserve funds would be practical.

Governor Vardaman commented on dangers envisaged by Governor Shepardson in the establishment of a special agency to administer a small business lending program and said that he saw more danger of creating a permanent bureaucracy by giving such powers to an established agency within the Government. While he agreed that the coordination of a small business lending program and Federal Reserve credit policy would create a problem, he suggested that to place in the Federal Reserve System a program involving political and social considerations would bring to bear on the System pressure to make decisions that could not be reached on purely economic grounds. He agreed with Governor Balderston that the capital and surplus of the Reserve Banks represented a target but suggested emphasizing that the residual interest in such funds was in the Treasury rather than in the member banks. As to the need for a comprehensive survey of small business financing problems, it was his view that the information most essential in appraising the situation could be obtained through the Federal Reserve Banks and branches in a relatively short period of time and that even the most comprehensive kind of survey would not be likely to provide conclusive answers.

Governor Mills stated that he did not feel quite as strongly as Governor Robertson about the use of "high-powered dollars" because the amount of funds involved under a program such as envisaged by S. 2160 would, relatively speaking, not be very substantial. In principle, however, he shared the views of Governor Robertson. With respect to the tone of the testimony, he noted the existence of a strong conviction in many quarters that private funds are not sufficiently available for the assistance of small business and that Federal funds therefore should be provided. While he felt that the Board should not go beyond encouraging the idea that private funds should be supplied wherever possible, the preliminary draft of testimony seemed to contend that the use of public funds should absolutely be precluded, whereas the very premise of S. 2160 was that private funds are not available in sufficient quantity.

Governor Szymczak, in an effort to establish what Board position on the furnishing of capital to national investment companies would be completely defensible, raised for consideration a series of questions relating to whether opposition to such use of the capital and surplus of the Federal Reserve Banks would be entirely compatible with the other uses of such funds, including the transfer of a major portion of Federal Reserve earnings to the Treasury.

From the foregoing and further discussion, it developed to be the general view of the Board that the testimony should maintain the basic position on financial assistance to small business that was expressed by the Board in testimony on the subject given in 1955. It was the prevailing feeling of the Board that discussion of the specific provisions of S. 2160 should be avoided as far as possible and that, although sympathy could be expressed with the objectives of the bill, the Federal Reserve System should not be called upon to provide the capital for the proposed national investment companies or to exercise supervision over them.

It was then agreed that another draft of testimony designed to reflect the tenor of the comments at this meeting would be prepared for consideration at the meeting of the Board tomorrow.

The meeting then adjourned.

Assistant Secretary