Minutes for July 3, 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 M	
Gov. Szymczak	x	
Gov. Vardaman	x	
Gov. Mills	x	
Gov. Robertson	x R	
Gov. Balderston	x CCB	
Gov. Shepardson	x	

Minutes of actions taken by the Board of Governors of the Federal Reserve System on Wednesday, July 3, 1957. The Board met in the Board Room at 10:00 a.m.

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

Mr. Carpenter, Secretary
Mr. Kenyon, Assistant Secretary
Mr. Thomas, Economic Adviser to the Board
Mr. Hackley, General Counsel
Mr. Masters, Director, Division of Examinations
Mr. Cherry, Legislative Counsel
Mr. Molony, Special Assistant to the Board
Mr. Koch, Assistant Director, Division of Research and Statistics
Mr. Hostrup, Assistant Director, Division of Examinations

Report on H.R. 8267 (Item No. 1). Pursuant to the understanding at the meeting of the Board yesterday, there had been distributed copies of a revised draft of letter to the Chairman of the House Committee on Government Operations concerning H.R. 8267, a bill which would establish a new independent agency of the Government with responsibility for studying and reporting on relationships between prices, profits, and wages, hidden taxes on products and services, and all factors responsible for inflation and deflation, and also for holding an annual conference of consumers for the purpose of exploring the causes of and solutions for inflation.

Following a brief discussion, the letter was approved unanimously, with the understanding that a copy would be sent to the Bureau of the Budget. A copy of the approved letter is attached to these minutes as Item No. 1.

Response to questions raised by Senator Clark (Item No. 2). Before this meeting there had been sent to the members of the Board copies of a revised draft of letter to Senator Clark responding to certain questions which the Senator had raised with Chairman Martin concerning the financing needs of small businesses and the effects of monetary and credit policy. The revised draft was intended to reflect comments made by members of the Board during discussion of the original draft at yesterday's meeting.

Following a discussion of the proposed reply, during which certain additional changes were agreed upon, unanimous approval was given to a letter to Senator Clark in the form attached to these minutes as Item No. 2.

Messrs. Thomas and Koch then withdrew from the meeting.

Request of Otto Bremer Company for a determination under the Bank Holding Company Act. In a memorandum dated July 2, 1957, which had been distributed to the members of the Board, Mr. Hackley reported that Otto Bremer Company of St. Paul, Minnesota, had requested a determination as to whether certain of its subsidiaries were exempt from the divestment provisions of section 4 of the Bank Holding Company Act. Under section 4(c)(6) of the Act, a hearing with respect to the request was mandatory, and the memorandum suggested arrangements which might be made for the hearing. With respect to the services of a Hearing Examiner, it was suggested that arrangements be worked out with the National Labor Relations Board for an extension for six months, beginning August 1, 1957, of the detail of Mr. Arthur Leff to act as Hearing Examiner in connection with hearings ordered by the Board pursuant to the Bank Holding Company Act. The memorandum also suggested that Mr. Sigurd Ueland, Vice President and Counsel of the Federal Reserve Bank of Minneapolis, be invited to act in the capacity of Board Counsel for the purpose of the prospective Otto Bremer hearing and that arrangements be made to have Mr. Ueland receive assistance from either Mr. G. W. Lamphere, Assistant General Counsel for the Federal Reserve Bank of Chicago, or Mr. Gerald T. Dunne, Counsel for the Federal Reserve Bank of St. Louis. When the foregoing arrangements had been completed, along with arrangements as to the time and place of the hearing, the Board would be advised. Formal notice of the date and place of the hearing would then be given to Otto Bremer Company and placed in the Federal Register.

Following comments on the matter by Mr. Hackley, unanimous agreement was expressed with the procedures suggested in the memorandum, with the understanding that if Mr. Ueland was not in a position to serve in the capacity of Board Counsel in connection with this hearing, Mr. M. H. Strothman, Jr., Vice President of the Minneapolis Reserve Bank, would be invited to serve in that capacity.

In this connection, Governor Robertson said that he had spoken to the President of each Federal Reserve Bank whose staff members had served as Board Counsel for the purpose of hearings of this kind, that the Presidents had expressed willingness to have their staff members serve in this capacity, and that he had told the Presidents to advise if it became difficult at any time to spare the persons concerned from their regular duties in response to further requests. In the case of Mr. Lamphere, he suggested that the Legal Division be guided by the advice of President Allen of the Chicago Reserve Bank as to whether Mr. Lamphere could conveniently be spared to assist in the Otto Bremer Company hearing.

The members of the staff then withdrew and the Board went into executive session.

Appointment of committee to study Retirement System matters. In a memorandum dated July 2, 1957, which had been distributed to the members of the Board, Governor Szymczak advised that, as requested by the Board at the meeting on June 26, 1957, he had considered the desirability of appointing a committee of consultants to review problems raised during discussion of the Board and Bank Plans of the Retirement System of the Federal Reserve Banks and had concluded that a valuable purpose would be served. The objective of such a study would be to provide a concise statement in nontechnical language, preferably in question and answer form, for the information and use of the Board and its staff, particularly in answering questions regarding the Retirement System whenever the occasion might arise. It was suggested that the study be in two parts, the first of which would relate to the underlying philosophy of the Retirement System and the second of which would set forth in non-technical language information about the retirement plans used in the Federal Reserve that would be helpful in comparing such plans with other retirement systems, including Civil Service. After discussing the qualifications that should be sought in members of such a committee, Governor Szymczak's memorandum recommended that Messrs. Leslie R. Rounds, Chester Morrill, and George B. Vest be appointed as a committee of consultants effective upon approval by the Board for a period not to exceed 30 days. The appointments would be on a contractual basis, with compensation at the rate of $50 per day for each day worked for the Board either in Washington or outside the city, plus a per diem in lieu of subsistence for the amount of time spent in travel status in connection with this assignment, and transportation, both in accordance with the Board's travel regulations.

The Secretary's Office later was informed by Governor Szymczak that during the executive session the Board approved the recommendation contained in his memorandum, with the understanding that Mr. Rounds would serve as Chairman of the committee, that the Board would provide necessary secretarial help and working space for the committee and would pay incidental expenses connected with the study and preparation of the report, and that the committee would have access to Retirement System records and data pertinent to its study.

The meeting then adjourned.

Secretary's Note: On July 2, 1957, Governor Shepardson approved on behalf of the Board a letter to the Federal Reserve Bank of New York approving the appointment of Messrs. Clark, Dearnley, Hinman, and Kober as assistant examiners. A copy of the letter is attached hereto as Item No. 3.

Secretary

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

Item No. 1
7/3/57

OFFICE OF THE CHAIRMAN

July 3, 1957

The Honorable William L. Dawson, Chairman,
Committee on Government Operations,
House of Representatives,
Washington 25, D. C.

Dear Mr. Dawson:

This is in reply to your letter of June 24 requesting comments on the bill H. R. 8267, which would establish a new independent agency, the Consumers Protective Bureau, with responsibility for studying and reporting on relationships between prices, profits and wages, hidden taxes on products and services, and all factors responsible for inflation or deflation, and also for holding an annual conference of consumers for the purpose of exploring the causes and solutions for inflation.

The Board is in full accord with the broad purposes of the bill, both with respect to its recognition of the importance of protecting consumers' interests and of the need for developing greater understanding of the causes of inflation and its effects on consumer welfare. However, the Board believes that it is unnecessary and would be inadvisable to create a new agency of the Government for these purposes. If studies along the lines indicated are considered desirable, it would be preferable, in the Board's opinion, for them to be made by the Congress itself or by some appropriate existing agency of the Government designated by the Congress.

Sincerely yours,

(Signed) Wm. McC. Martin, Jr.

Wm. McC. Martin, Jr.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

Item No. 2
7/3/57

OFFICE OF THE CHAIRMAN

July 3, 1957

The Honorable Joseph S. Clark,
United States Senate,
Washington 25, D. C.

Dear Senator Clark:

In your letter of June 24 you asked for my comment on a number of questions. I am happy to comment, and hope that my responses will be useful to you and your Committee.

1. Do you agree that "tighter credit conditions affected unevenly different sectors of the economy and different types of businesses"?

2. Is an uneven effect of credit and monetary policy bad for the economy as a whole?

These questions are closely related and I shall try to answer them together.

In an economy as broad and as interdependent as ours, the effects of tighter credit tend to be pervasive--more so, I think, than is commonly realized. One of the immediate effects is to increase the cost of credit thereby tending to reduce the volume of borrowing. It also increases the rewards for savings thereby increasing the amount of loanable funds available. These influences spread throughout the economy in a relatively short time.

To take one example, if individuals decide to save more or borrow less by reducing their purchases of durable goods, these decisions affect several very large and important industries in the country--industries which include both giant manufacturers and relatively small dealers, as well as companies that customarily depend heavily on borrowed funds and those that rely more extensively on internal financing. The decisions also affect the availability of loanable funds to a variety of lenders and hence their ability to meet their customers' demands. In short, these decisions affect in one way or another the countless saving, spending, lending and borrowing activities that make up our daily economic and business life.

One cannot say that every activity, every sector, every member of every sector in the economy is evenly affected by tight credit conditions. Neither can one determine the extent to which one sector is affected relative to another. There is unquestionably some unevenness in the effect of general monetary restraints, but the alternatives--unrestrained inflation or a harness of specific direct controls--would in my opinion be immeasurably more uneven in their discriminatory effects.

3. In general, do higher interest rates and a reduced supply of credit in relation to demand pose more serious problems for small businesses than for large businesses?

It is difficult to say whether, and if so to what extent, tight credit conditions by themselves have a disproportionately adverse effect on small businesses. So far as short-term bank credit is concerned--and small businesses rely heavily on this type of credit--the information we receive from surveys suggests that the supply of such credit has not diminished over the past two and one-half years. While interest rates on small loans of banks generally are higher than rates on large loans, the increase in rates on small loans has been less than that on large loans over this period. Small businesses have also had an increased volume of internal funds and this may have moderated their needs for borrowed funds. According to F.T.C.-S.E.C. data for manufacturing corporations, the profits of small companies increased substantially in 1956, compared with a decline for large companies.

The financing problem of small businesses lies, in our judgment, in the field of long-term debt and equity capital. To some extent, higher interest rates and a supply of credit short of demand for its use may intensify this problem.

It is in boom times that the demands for the goods and services of small, as well as large, businesses are at their peak. It is then that businesses are tempted to overestimate their future growth, to overextend themselves, and to lay the seeds for trouble when final demand is less pressing. Some small businesses, without the research and technical advisory services available to many larger firms, are particularly vulnerable to such miscalculations. The fact that business enterprises may be restrained in their expansion by reluctance on the part of investors to make all of the capital they want available to them is one of the "checks and balances" in our economic system which helps to prevent uneconomic use of our resources.

4. On the basis of such factual information as may be available to you, what additional volume of credit to small businesses would be necessary to maintain their fair share of the total quantity of credit available?

So far as I know, there is no factual information available that would permit a satisfactory judgment as to the amount of credit that represents small business' "fair share." If one accepts the premise that the impersonal judgment of the market place, while economic in the broadest sense, does not always satisfy desirable social objectives, then one must set up different criteria for allocating available credit. This might result in further involving the Federal Government in financial activities beyond the scope of its ordinary responsibilities. Moreover, these criteria would have to be very general and would have to be geared to the broad social objectives desired rather than to any particular dollar or percentage amounts. This would be a most difficult task and I do not believe it would be as effective as the judgment of the market place.

5. If this additional volume is greater than the lending authority of the Small Business Administration, how can the supply of credit for small businesses be increased?

7. Is it feasible to increase the supply of credit available to small businesses solely through the lending program of the Small Business Administration?

I can also answer these related questions together. Since I feel that it is extremely difficult to determine the "fair share" of the aggregate credit pool that small businesses should receive without the guidance of the market place, I find it equally as difficult to say whether the Small Business Administration can adequately fill any gap that may exist between the "fair share" and the amount of credit currently available to small firms.

As I indicated in my testimony, if there is such a gap, every effort should be made to encourage private organizations to fill it.

6. Could the Board of Governors of the Federal Reserve System take steps to increase the supply of credit for small businesses through policy statements or advice to member-institutions?

The Federal Reserve System has studiously avoided interfering with the operations of its member banks in allocating the available supply of credit to particular sectors or individual members of the economy. This allocation is best left to market forces and to the decisions of our numerous, widely scattered, and locally oriented commercial banks. The Federal Reserve concentrates on influencing the over-all quantity of money and credit and on trying to keep their growth consistent with the maintenance of orderly economic progress.

8. When the Congress attempts to alleviate the uneven effects of policies which restrain credit, it is frequently said that such attempts are inflationary. If the Congress decides that such direct lending programs are essential, cannot the Federal Reserve System take action through open market operations or other means to offset any inflationary tendencies which might otherwise result?

The Federal Reserve would, of course, do everything within its power, through open market operations or other means, to offset any inflationary tendencies that might arise from direct Government lending programs. Such offsetting action is very difficult to accomplish, however, and might prove relatively ineffective, at least in the short-run, due both to the problem of measuring the potential inflationary effects of particular lending programs and the fact that the effects of offsetting action would be delayed. The most appropriate way to counteract this type of inflationary pressure would be through fiscal policy, that is, by financing any new specialized lending programs by taxation.

Sincerely yours,

Wm McC. Martin, Jr.

Wm. McC. Martin, Jr.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON 25, D. C.

Item No. 3
7/3/57

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

July 2, 1957

Mr. A. Phelan, Vice President,
Federal Reserve Bank of New York,
New York 45, New York.

Dear Mr. Phelan:

In accordance with the request contained in your letter of June 26, 1957, the Board approves the appointment of William A. Clark, Robert W. Dearnley, William J. Hinman and Dale G. Kober as assistant examiners for the Federal Reserve Bank of New York. If the appointments are not made effective July 8, 1957, as planned, please advise us.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Assistant Secretary.