MINUTES OF THE MEETING OF THE FEDERAL ADVISORY COUNCIL

May 17, 1953

The second statutory meeting of the Federal Advisory Council for 1953 was convened in Room 736 of the Mayflower Hotel, Washington, D. C., on May 17, 1953, at 2:20 P.M., the President, Mr. Brown, in the Chair.

Present:

Ernest Clayton	District No. 1
Henry C. Alexander	District No. 2
Geoffrey S. Smith	District No. 3
Robert V. Fleming	District No. 5
Paul M. Davis	District No. 6
Edward E. Brown	District No. 7
V. J. Alexander	District No. 8
Joseph F. Ringland	District No. 9
Charles J. Chandler	District No. 10
De Witt Ray	District No. 11
John M. Wallace	District No. 12
Herbert V. Prochnow	Secretary

Absent:

George Gund	District No. 4

On motion duly made and seconded, the mimeographed notes of the meeting held on February 15, 16, 17, 1953, copies of which had been sent previously to the members of the Council, were approved.

A complete list of the items on the agenda for the meeting, and the conclusions of the Council are to be found in the *Confidential Memorandum to the Board of Governors from the Federal Advisory Council,* which follows on pages 15, 16 and 17.

The meeting adjourned at 5:40 P.M.

HERBERT V. PROCHNOW
Secretary

MINUTES OF THE MEETING OF THE FEDERAL ADVISORY COUNCIL

May 18, 1953

At 10:00 A.M., the Federal Advisory Council reconvened in Room 736 of the Mayflower Hotel, Washington, D. C.

Present: Mr. Edward E. Brown, President; Messrs. Ernest Clayton, Henry C. Alexander, Geoffrey S. Smith, George Gund, Robert V. Fleming, Paul M. Davis, V. J. Alexander, Joseph F. Ringland, Charles J. Chandler, De Witt Ray, John M. Wallace, and Herbert V. Prochnow, Secretary.

The Council reviewed its conclusions of the previous day regarding the items on the agenda, and sent to the Secretary of the Board of Governors the *Confidential Memorandum* which follows on pages 15, 16 and 17, listing the agenda items with the conclusions reached by the Council. The *Memorandum* was delivered to the Secretary of the Board of Governors at 11:55 A.M. on May 18, 1953.

The meeting adjourned at 11:40 A.M.

HERBERT V. PROCHNOW
Secretary

MEMORANDUM TO THE BOARD OF GOVERNORS FROM THE FEDERAL ADVISORY COUNCIL RELATIVE TO THE AGENDA FOR THE JOINT MEETING ON MAY 19, 1953

1. What are the views of the Council with respect to the prospective business situation during the next six months and the probable changes in the volume and purposes of bank loans in that period including commercial, consumer and real estate loans?

Business continues to operate at a high level, although spottiness and evidences of weakness exist in a few industries. The gross national product and personal income are at peacetime highs. Industrial production is very large, particularly in durable manufactures. The production of various nondurable goods has improved since last year. Perhaps the most notable increase in production over a year ago is to be found in the automobile industry, but the present large production, combined with the large automobile inventory both of new and used cars at retail levels, may cause weakness in the latter half of the year. Despite the large production of household durables, there is evidence that demand in some lines may not be sufficient to absorb present output. Employment generally continues at record levels. Although the rate of increase in business inventories has slackened, stocks have risen to new peaks. The outlook for the agricultural industry depends to a considerable extent upon weather conditions in the weeks and months immediately ahead. The coal industry and prices for base metals are depressed, with the probability that copper prices may also decline.

Despite widespread prosperity and a high rate of business activity, there is more general apprehension regarding the business outlook than there has been at any time in the past few years. This apprehension would tend to intensify a downward economic trend, should one occur. A majority of the Council believes that the probability is for a moderate down-turn in business in the next six months. A minority of the Council believes that no appreciable down-turn in business as a whole will occur in this period.

The views of the Council relative to the probable trend in loans and the related subject of System credit policies will be found in the answer to Items 2 and 3 of the Agenda.

2. What comments does the Council have to make with respect to (a) the System's credit policies in the months ahead, and (b) the steps that might be taken in the field of credit policy in the event of a change in the economic climate?

3. In view of the continuing demands for credit on all types of lenders and the plans of business for continued need for credit, and in the light of the Treasury's needs not only for refunding but for new cash during the next six months, and with bank deposits throughout the nation considerably off due to the Mills Plan requiring accelerated tax payments by corporations, together with the higher bill rate (making it look likely that bank deposits will not return in appreciable volume until late in the year and many corporations may be tempted to place their funds in Treasury Bills rather than deposit them in the banking

system) and with seasonal loans rising in the Fall, the Council would like to have the views of the Board and Open Market Committee as to their views on easing credit conditions, assuming that bank loans will continue at present levels, deposits will not return to the banking system as rapidly as heretofore, and seasonal loans will in all probability be superimposed on the present high loan level.

Because Items 2 and 3 of the Agenda are closely related, the Council has treated them as one item in its answer.

While business loans have shown some seasonal decline, the demand for credit of all types—commercial, consumer and construction—is strong. The Council believes that this demand will continue, barring a marked turn down in business, and will have added to it in the late summer and fall the usual seasonal demands which must be met.

In view of the present tightness in the money market, apprehension over the availability of credit, fear of materially higher rates, the requirements of the Treasury in the next few months including a virtual certainty of a considerable amount of deficit financing, and the coming seasonal demand for loans, the Council believes that some relief should now be given the money market. So long as business activity continues at present levels, relief should be given by open market operations through the purchase of short-term securities. The rate and extent of such relief would naturally vary from week to week. Favorable consideration should also be given to an early reduction in Central Reserve City reserve requirements, since such cities are the principal money markets, and a reduction there would have an immediate effect.

Should business begin to decline, with a reduction in retail sales, the volume of bank loans will nevertheless continue high during the time required to liquidate inventories. In the event of a business down-turn, the System should ease the money market considerably. This should be done by stepping up open market purchases of short-term securities and by a reduction of reserve requirements for all classes of banks. If the down-turn in business should prove temporary and an upturn follow, sales for open market account could be used in the first instance to adjust the situation.

Since there is always some lag between any action of the System and its effect on the economy, action to relieve the situation in the money market, both now and in the event of a business down-turn, should not be delayed.

As a corollary to the Council's suggestion that the System should now relieve the tightness in the money market, the Council believes that no increase should be made now in the rediscount rate. Such an increase would largely offset the effect of other System actions.

4. The proposal is being advanced in the Congress that the Reconstruction Finance Corporation be abolished and that some arrangement be made through the Federal Reserve Banks or otherwise for the extension of loans, particularly to small business, which would not be available through the regular banking channels. The Board would like to have the views of the Council on this proposal and, if thought desirable, the manner in which it might best be carried out.

The function of a central banking system is the responsibility of dealing with the broad problem of monetary management, as it relates especially to the money supply. That important responsibility should not be confused by associating it with other functions which may be discharged by other agencies in the economy. If an agency is to be given authority to extend loans to small business, finance defense industries, or provide loans in times of emergency or disaster, when credit may not be available through ordinary banking channels, the agency should not be connected or associated with the Federal Reserve System.

Restating the view it has held in the past, the Council also believes in this connection that Section 13b of the Federal Reserve Act should be eliminated.

MINUTES OF THE MEETING OF THE FEDERAL ADVISORY COUNCIL

May 18, 1953

At 2:05 P.M., the Federal Advisory Council convened in the Board Room of the Federal Reserve Building, Washington, D. C., the President, Mr. Brown, in the Chair.

Present: Mr. Edward E. Brown, President; Messrs. Ernest Clayton, Henry C. Alexander, Geoffrey S. Smith, George Gund, Robert V. Fleming, Paul M. Davis, V. J. Alexander, Joseph F. Ringland, Charles J. Chandler, De Witt Ray, John M. Wallace, and Herbert V. Prochnow, Secretary. Governor Cobbold of the Bank of England was also present, as well as economists associated with the Open Market Committee.

Dr. Woodlief Thomas, Economic Adviser to the Board; Dr. Ralph A. Young, Director of the Division of Research and Statistics; and Frank R. Garfield, Adviser on Economic Research, together with members of the staff, presented a visual-audio report on the economic and business situation.

The meeting adjourned at 4 P.M.

HERBERT V. PROCHNOW
Secretary

MINUTES OF JOINT CONFERENCE OF THE FEDERAL ADVISORY COUNCIL AND THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

May 19, 1953

At 10:32 A.M., a joint conference of the Federal Advisory Council and the Board of Governors of the Federal Reserve System was held in the Board Room of the Federal Reserve Building, Washington, D. C.

Present: Members of the Board of Governors of the Federal Reserve System:

Chairman Wm. McC. Martin, Jr.; Governors M. S. Szymczak, R. M. Evans, James K. Vardaman, Jr., and J. L. Robertson; also Mr. S. R. Carpenter, Secretary, and Mr. Merritt Sherman, Assistant Secretary of the Board of Governors.

Present: Members of the Federal Advisory Council:

Mr. Edward E. Brown, President; Messrs. Ernest Clayton, Henry C. Alexander, Geoffrey S. Smith, George Gund, Robert V. Fleming, Paul M. Davis, V. J. Alexander, Joseph F. Ringland, Charles J. Chandler, De Witt Ray, John M. Wallace and Herbert V. Prochnow, Secretary.

The President of the Council read the first item of the agenda and the conclusions of the Council as given in the *Confidential Memorandum to the Board of Governors from the Federal Advisory Council*, as printed on pages 15, 16 and 17 of these minutes.

A discussion followed in which members of the Council and the Board participated.

The President of the Council read the second and third items on the agenda and the conclusions of the Council given in the *Confidential Memorandum* mentioned above. President Brown added that the members of the Council differ with Chairman Martin's recent statement that banks should anticipate their seasonal needs. The President believes it was understood, at the time of the establishment of the Federal Reserve System, that the System should provide funds for the seasonal needs of banks.

A discussion, participated in by members of the Board and the Council, followed.

President Brown read the fourth item on the agenda and the conclusions of the Council as stated in the *Confidential Memorandum* previously mentioned. A brief discussion followed.

Chairman Martin reported that the comments of the Council have been very helpful.

The meeting adjourned at 12:35 P.M.

HERBERT V. PROCHNOW
Secretary

NOTE: This transcript of the Secretary's notes is not to be regarded as complete or necessarily entirely accurate. The transcript is for the sole use of the members of the Federal Advisory Council. The concise official minutes for the entire year are printed and distributed later.

H. V. P.

The Secretary's notes on the meeting of the Federal Advisory Council on May 17th, 1953 at 2:20 P. M. in Room 736 of the Mayflower Hotel, Washington, D. C. All members of the Federal Advisory Council were present except Mr. Gund, who was unavoidably absent because of illness in his family.

The Council approved the Secretary's notes for the meeting of February 15-17, 1953.

* * * *

ITEM I

WHAT ARE THE VIEWS OF THE COUNCIL WITH RESPECT TO THE PROSPECTIVE BUSINESS SITUATION DURING THE NEXT SIX MONTHS AND THE PROBABLE CHANGES IN THE VOLUME AND PURPOSES OF BANK LOANS IN THAT PERIOD INCLUDING COMMERCIAL, CONSUMER AND REAL ESTATE LOANS?

Brown asks each member of the Council to express his views on the business outlook in his district.

Clayton. Production in the district is high. Textiles have strengthened compared to a year ago. Bank loans are higher than last year, but deposits are down. Construction may establish new records. Automobile sales of new cars are high. There is some pessimism in the used car market. Hard goods are somewhat slow. There is a possibility that business may experience some decline rather quickly, but at the present time business is good.

H. Alexander. Business activity continues at a very high level. More people are employed. Most of the increase in employment is in the metal working industry. The apparel industries are a little better than a year ago. Inventories are high in dollars, but in relation to present sales, are not abnormal. Construction is active. The demand for money is pressing and banks are tight. Deposits in the district are down since the first of the year and also from last year. Business generally is good.

Smith reports that conditions in his district are essentially the same as those reported by Clayton and Alexander. Business is operating at a high level. Both soft goods and durables are doing well. Sales of popular priced cars are especially good. Inventories are high in dollars but not in relation to present sales. Commercial loans are down, but they have declined less than seasonally. The Mills Plan may have altered the normal seasonal pattern of loans and deposits. Loans should tend to run off unless the Mills Plan holds them up.

Fleming. Business generally is up everywhere in his district. Overall retail sales are higher. The furniture business is good in North Carolina, which state now is the leader in furniture manufacturing. Deposits are up from a year ago, but down from the end of 1952. Borrowings from the Federal Reserve have increased. Demands for credit are pressing. Fleming has heard many optimistic reports from business leaders regarding the outlook. The farm implement industry may have some problems. However, business generally is good.

Davis. Business is very active. Employment is at a high level. There are some signs of overproduction. The textile industry is better than it was a year ago. Steel and iron are very good. Loans are not as tight in his district as they are in some others. There is considerable uneasiness, although 1953 looks about as good now as 1952.

V. Alexander believes business generally is good. Employment is high. There is a heavy demand for money. Consumer credit is up. Small finance companies have run out of money. The spring weather has not been good as it has been raining almost a solid month. New cars are coming into the district in large numbers. Alexander is concerned about the new car market continuing good. The used car market is bad. Deposits are a little above last year. Retail trade is good. There is some uneasiness and concern about the future. Alexander expects the usual seasonal loan demand.

Ringland. Business is good. There was not any too much snow or rain this winter, but in the last six weeks there has been considerable moisture and the crop outlook is better. Deposits are about the same as a year ago. The deposits of bank correspondents are down. Loans are higher and money is fairly tight. Ringland believes conditions in his territory will be about as good as they were last year.

Chandler. Labor conditions are good. Wichita has a labor shortage due to Boeing, but Boeing has now quit hiring. Deposits are about the same as a year ago. Moisture conditions are better in the eastern part of his territory than in the western part. The cattle situation is not satisfactory and does not look hopeful. In general, any agricultural product in his district that is not supported by the government is down in price. Agricultural income in 1953 will probably be lower. Money conditions are relatively easy in the district compared to the country as a whole.

Ray. Business is generally good but there is some spottiness due to the weather. There have been heavy rains in some sections, particularly in the eastern part of his district. The wheat situation is not good. There are large losses in the cattle industry, although Ray knows of no distress sales. Department store sales are holding up well. New automobile sales are good, but the used car market is slow. The "off-brands" of cars are not selling well. The better known car brands have been doing well, but inventories are high. Oil production is down. Construction is good in the residential field, but industrial construction is down. Ray is hesitant about forecasting the future, as it depends on weather conditions. Deposits are down, compared to a year ago but loans are up. The volume of merchants' receivables is high. There is a good deal of apprehension regarding the future. There is a possibility of a decline in business in the next six months but loans may go up because of agricultural loan demands. (At this point there were off-the-record comments).

Wallace. Loans are at peak levels in the inter-mountain country. Correspondent banks are coming to the larger banks for help in carrying loans. Deposits are about the same as a year ago. The situation in the lead and zinc industries is not good. More natural gas is being produced in the district and some is being shipped out. Oil may be brought into the northwest part of the district from Canada with the result that industrial development would be strongly stimulated. In the southern part of his district there is a danger of a shortage of water over a long period. Business generally in the district is good and should continue active for the balance of the year. However, if peace should come in Asia, there will probably be a rather large decline in the freight moving out of this district to the war area.

Brown. Conditions in the Seventh district are essentially similar to those in the other districts. Manufacturing is at a high level. The agricultural implement industry may be faced with difficulty, and there may also be some decline in freight car construction. Used car prices are down. Hard goods have been moving quite well, but there are some evidences now of a little slowness in this field. The steel industry is very active, and the whole level of business is high. Deposits are up from a year ago, but are down from the year-end. The demand for consumer credit seems unlimited. Loans will probably stay about where they are plus the usual fall increase. (Off the record comments). There is more uneasiness about the business outlook than there has been for some time.

Chandler asks if there is apprehension in other districts among leaders in industry and business about the outlook.

Fleming comments that the redemptions in savings bonds have recently exceeded the sales.

Brown. Some producers of hard goods have cut back production.

V. Alexander. The farmers are pessimistic. They see the wages of labor increasing while the prices of farm products are declining.

Davis. (Off-the-record comments)

Brown. The Council may say that business generally continues at a high level, but there is spottiness in some industries. Personal income and employment are high. The Council may also state that there is more apprehension regarding the business outlook than there has been for the past two years. That apprehension would magnify any downturn. In agriculture much will depend on the weather. Brown asks for a show of hands of those who believe that there may be a moderate downturn in business in the next six months. A majority of the Council believes there will be a moderate downturn, but the minority feels there will be no appreciable downturn of business in the next six months.

Wallace. Copper prices will probably follow down the prices of other base metals.

Brown. The base metals and coal are depressed.

ITEM II

WHAT COMMENTS DOES THE COUNCIL HAVE TO MAKE WITH RESPECT TO (a) THE SYSTEM'S CREDIT POLICIES IN THE MONTHS AHEAD, AND (b) THE STEPS THAT MIGHT BE TAKEN IN THE FIELD OF CREDIT POLICY IN THE EVENT OF A CHANGE IN THE ECONOMIC CLIMATE?

ITEM III

IN VIEW OF THE CONTINUING DEMANDS FOR CREDIT ON ALL TYPES OF LENDERS AND THE PLANS OF BUSINESS FOR CONTINUED NEED FOR CREDIT, AND IN THE LIGHT OF THE TREASURY'S NEEDS NOT ONLY FOR REFUNDING BUT FOR NEW CASH DURING THE NEXT SIX MONTHS, AND WITH BANK DEPOSITS THROUGHOUT THE NATION CONSIDERABLY OFF DUE TO THE MILLS PLAN REQUIRING ACCELERATED TAX PAYMENTS BY CORPORATIONS, TOGETHER WITH THE HIGHER BILL RATE (MAKING IT LOOK LIKELY THAT BANK DEPOSITS WILL NOT RETURN IN APPRECIABLE VOLUME UNTIL LATE IN THE YEAR AND MANY CORPORATIONS MAY BE TEMPTED TO PLACE THEIR FUNDS IN TREASURY BILLS RATHER THAN DEPOSIT THEM IN THE BANKING SYSTEM) AND WITH SEASONAL LOANS RISING IN THE FALL, THE COUNCIL WOULD LIKE TO HAVE THE VIEWS OF THE BOARD AND OPEN MARKET COMMITTEE AS TO THEIR VIEWS ON EASING CREDIT CONDITIONS, ASSUMING THAT BANK LOANS WILL CONTINUE AT PRESENT LEVELS, DEPOSITS WILL NOT RETURN TO THE BANKING SYSTEM AS RAPIDLY AS HERETOFORE, AND SEASONAL LOANS WILL IN ALL PROBABILITY BE SUPERIMPOSED ON THE PRESENT HIGH LOAN LEVEL.

Fleming thinks the Federal Reserve System will have to buy bills in order to hold the money market where it is now. He would like to see the money market eased somewhat. He believes it is certain the banks will not have the funds to finance both the fall seasonal demands and the Treasury needs.

H. Alexander. (Comments off-the-record, on the federal deficit)

Fleming states that for the remainder of the calendar year $27 billion of marketable obligations are to be refinanced.

Brown raises the question of whether the large volume of Treasury bills now held by corporations presents a situation comparable to the funds corporations had placed in the call money market in the 1920's. If corporations should ever decide to dispose of their Treasury bills, it might present a major problem.

H. Alexander states that in February he felt money should be tightened, and he believes that conclusion was correct at that time. However, the situation has now changed, and money is very tight and interest rates are up. (Off-the-record comments). He believes there is a possibility of a downward trend in business in the next six months. He also thinks the System should make money a little more available. He recommends lowering reserves somewhat, at least in New York and Chicago, where money is especially tight.

Brown. Assuming there is no change in general conditions, the System should ease the strain in the money market through open market purchases of short term issues.

Ringland. If the banks are under pressure not to borrow from the System, the banks may disrupt the money markets more by selling securities than by rediscounting.

Brown. (Off-the-record comments on rediscounting)

H. Alexander. (Off-the-record comments on rediscounting)

(At this point there were off-the-record comments from a number of members.)

Fleming believes it is time for the System to reexamine its whole credit policy in view of Treasury needs, the seasonal demand for bank loans, the extreme tightness of the money markets and the decline in bank deposits.

Brown. Assuming a continuance of present economic conditions - - the present tightness of money, and the unsettled conditions in the money market require some relief through open market operations. If business should turn down, the demand for loans will continue during the time required to liquidate inventories. If open market activities are increased, the System should operate in the short-term market and not in the long term market.

Fleming. (Off-the-record comments)

Brown. (Off-the-record comments)

Smith. Since action by the System takes time before its effect is felt in the economy, the System should not hesitate too long. There is always a lag between action by the System and its effect. Action should be taken at the first major sign of a decline.

Brown asks members of the Council their views regarding the rediscount rate, and all members indicate they are in favor of no change in the rediscount rate at present.

H. Alexander. The rediscount rate should not be raised now.

Brown. As a corollary to the Council's recommendation that the Federal Reserve System should put a small amount of funds in the market, and, in the event of a downturn, should step up the open market purchases rapidly, the Council may state that the rediscount rate should not be increased now as the psychological effect might be bad.

ITEM IV

THE PROPOSAL IS BEING ADVANCED IN THE CONGRESS THAT THE RECONSTRUCTION FINANCE CORPORATION BE ABOLISHED AND THAT SOME ARRANGEMENT BE MADE THROUGH THE FEDERAL RESERVE BANKS OR OTHERWISE FOR THE EXTENSION OF LOANS, PARTICULARLY TO SMALL BUSINESS, WHICH WOULD NOT BE AVAILABLE THROUGH THE REGULAR BANKING CHANNELS. THE BOARD WOULD LIKE TO HAVE THE VIEWS OF THE COUNCIL ON THIS PROPOSAL AND, IF THOUGHT DESIRABLE, THE MANNER IN WHICH IT MIGHT BEST BE CARRIED OUT.

Brown does not believe the System should have anything to do with any organization set up to extend loans to small business.

Wallace thinks it might be advisable to keep the R. F. C. rather than to set up another organization.

Brown believes that any proposed organization to finance small business should not be tied in with the Federal Reserve System. The Council may say that it is unanimously of the opinion that if an agency is established to extend loans to small business, finance defense industries, or provide loans in times of emergency or disaster, when credit may not be available through ordinary banking channels, that agency should not be connected or associated with the Federal Reserve System. The Council may also state, as it has in the past, that Section 13b of the Federal Reserve Act should be eliminated.

The meeting adjourned at 5:40 P. M.

THE COUNCIL CONVENED AT 10 A. M. ON MAY 18, 1953, IN ROOM 736 OF THE MAYFLOWER HOTEL, WASHINGTON, D. C. ALL MEMBERS OF THE FEDERAL ADVISORY COUNCIL WERE PRESENT.

The Council prepared and approved the attached Confidential Memorandum to be sent to the Board of Governors relative to the agenda for the joint meeting of the Council and the Board on May 19, 1953. The Memorandum was delivered to the Secretary of the Board of Governors at 11:55 A. M. on May 18, 1953. It will be noted that each item of the agenda is listed together with the comments of the Council.

The meeting adjourned at 11:40 A. M.

CONFIDENTIAL

MEMORANDUM TO THE BOARD OF GOVERNORS
FROM THE
FEDERAL ADVISORY COUNCIL
RELATIVE TO THE AGENDA FOR THE JOINT MEETING
ON MAY 19, 1953

1. What are the views of the Council with respect to the prospective business situation during the next six months and the probable changes in the volume and purposes of bank loans in that period including commercial, consumer and real estate loans?

Business continues to operate at a high level, although spottiness and evidences of weakness exist in a few industries. The gross national product and personal income are at peacetime highs. Industrial production is very large, particularly in durable manufactures. The production of various nondurable goods has improved since last year. Perhaps the most notable increase in production over a year ago is to be found in the automobile industry, but the present large production, combined with the large automobile inventory both of new and used cars at retail levels, may cause weakness in the latter half of the year. Despite the large production of household durables, there is evidence that demand in some lines may not be sufficient to absorb present output. Employment generally continues at record levels. Although the rate of increase in business inventories has slackened, stocks have risen to new peaks. The outlook for the agricultural industry depends to a considerable extent upon weather conditions in the weeks and months immediately ahead. The coal industry and prices for base metals are depressed, with the probability that copper prices may also decline.

Despite widespread prosperity and a high rate of business activity, there is more general apprehension regarding the business outlook than there has been at any time in the past few years. This apprehension would tend to intensify a downward economic trend, should one occur. A majority of the Council believes that the probability is for a moderate down-turn in business in the next six months. A minority of the Council believes that no appreciable down-turn in business as a whole will occur in this period.

The views of the Council relative to the probable trend in loans and the related subject of System credit policies will be found in the answer to Items 2 and 3 of the Agenda.

2. What comments does the Council have to make with respect to (a) the System's credit policies in the months ahead, and (b) the steps that might be taken in the field of credit policy in the event of a change in the economic climate?

3. In view of the continuing demands for credit on all types of lenders and the plans of business for continued need for credit, and in the light of the Treasury's needs not only for refunding but for new cash during the next six months, and with bank deposits throughout the nation considerably off due to the Mills Plan requiring accelerated tax payments by corporations, together with the higher bill rate (making it look likely that bank deposits will not return in appreciable volume until late in the year and many corporations may be tempted to place their funds in Treasury Bills rather than deposit them in the banking system) and with seasonal loans rising in the Fall, the Council would like to have the views of the Board and Open Market Committee as to their views on easing credit conditions, assuming that bank loans will continue at present levels, deposits will not return to the banking system as rapidly as heretofore, and seasonal loans will in all probability be superimposed on the present high loan level.

Because Items 2 and 3 of the Agenda are closely related, the Council has treated them as one item in its answer.

While business loans have shown some seasonal decline, the demand for credit of all types--commercial, consumer and construction--is strong. The Council believes that this demand will continue, barring a marked turn down in business, and will have added to it in the late summer and fall the usual seasonal demands which must be met.

In view of the present tightness in the money market, apprehension over the availability of credit, fear of materially higher rates, the requirements of the Treasury in the next few months including a virtual certainty of a considerable amount of deficit financing, and the coming seasonal demand for loans, the Council believes that some relief should now be given the money market. So long as business activity continues at present levels, relief should be given by open market operations through the purchase of short-term securities. The rate and extent of such relief would naturally vary from week to week. Favorable consideration should also be given to an early reduction in Central Reserve City reserve requirements, since such cities are the principal money markets, and a reduction there would have an immediate effect.

Should business begin to decline, with a reduction in retail sales, the volume of bank loans will nevertheless continue high during the time required to liquidate inventories. In the event of a business down-turn, the System should ease the money market considerably. This should be done by stepping up open market purchases of short-term securities and by a reduction of reserve requirements for all classes of banks. If the down-turn in business should prove temporary and an upturn follow, sales for open market account could be used in the first instance to adjust the situation.

Since there is always some lag between any action of the System and its effect on the economy, action to relieve the situation in the money market, both now and in the event of a business down-turn, should not be delayed.

As a corollary to the Council's suggestion that the System should now relieve the tightness in the money market, the Council believes that no increase should be made now in the rediscount rate. Such an increase would largely offset the effect of other System actions.

4. The proposal is being advanced in the Congress that the Reconstruction Finance Corporation be abolished and that some arrangement be made through the Federal Reserve Banks or otherwise for the extension of loans, particularly to small business, which would not be available through the regular banking channels. The Board would like to have the views of the Council on this proposal and, if thought desirable, the manner in which it might best be carried out.

The function of a central banking system is the responsibility of dealing with the broad problem of monetary management, as it relates especially to the money supply. That important responsibility should not be confused by associating it with other functions which may be discharged by other agencies in the economy. If an agency is to be given authority to extend loans to small business, finance defense industries, or provide loans in times of emergency or disaster, when credit may not be available through ordinary banking channels, the agency should not be connected or associated with the Federal Reserve System.

Restating the view it has held in the past, the Council also believes in this connection that Section 13b of the Federal Reserve Act should be eliminated.

THE COUNCIL CONVENED IN THE BOARD ROOM OF THE FEDERAL RESERVE BUILDING AT 2:05 P. M. ON MAY 18, 1953. ALL MEMBERS OF THE FEDERAL ADVISORY COUNCIL WERE PRESENT. GOVERNOR COBBOLD OF THE BANK OF ENGLAND WAS ALSO PRESENT, AS WELL AS ECONOMISTS ASSOCIATED WITH THE OPEN MARKET COMMITTEE.

Dr. Woodlief Thomas, Economic Adviser to the Board, Dr. Ralph A. Young, Director of the Division of Research and Statistics and Frank R. Garfield, Adviser on Economic Research, together with members of the staff, presented a visual-audio report on the economic and business situation. Copies of the report were not available for distribution.

The meeting adjourned at 4 P. M.

ON MAY 19, 1953, AT 10:32 A. M. THE FEDERAL ADVISORY COUNCIL HELD A JOINT MEETING WITH THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM IN THE BOARD ROOM OF THE FEDERAL RESERVE BUILDING, WASHINGTON, D. C.

ALL MEMBERS OF THE COUNCIL WERE PRESENT. THE FOLLOWING MEMBERS OF THE BOARD OF GOVERNORS WERE PRESENT: CHAIRMAN MARTIN, GOVERNORS SZYMCZAK, EVANS, VARDAMAN AND ROBERTSON. MR. CARPENTER, SECRETARY, AND MR. SHERMAN, ASSISTANT SECRETARY OF THE BOARD OF GOVERNORS, WERE ALSO PRESENT.

ITEM I

WHAT ARE THE VIEWS OF THE COUNCIL WITH RESPECT TO THE PROSPECTIVE BUSINESS SITUATION DURING THE NEXT SIX MONTHS AND THE PROBABLE CHANGES IN THE VOLUME AND PURPOSES OF BANK LOANS IN THAT PERIOD INCLUDING COMMERCIAL, CONSUMER AND REAL ESTATE LOANS?

Brown reads Item 1 of the agenda and the conclusions of the Council, as expressed in the Confidential Memorandum to the Board attached. It is a serious question whether the present annual output of automobiles can be sustained, as there is a possibility of a decline in automobile sales in the last half of the year. No member of the Council expects a serious downturn in business in the next six months, but a majority of the Council expect a moderate decline. A minority of the Council believe there will be no appreciable downturn in business in the next six months.

Fleming states that some lines of business may be spotty and there may be some reduction in the government budget. However, the budget will be unbalanced and deficit financing will take place. Fleming sees no threat of a serious decline.

Martin says there are so many conflicting views on the automobile situation that he would appreciate further comments on that industry. He asks whether it is a question of lower profits to automobile dealers.

H. Alexander believes that automobile sales will decline in the latter part of the year. A number of the members of the Council report that used car lots in their communities are filled with cars, and that the used car market is bad.

Ray reports that there is "bootlegging" at a discount of new cars from used car lots. It is not possible to trace these new cars to their dealer source. Some of the dealers unfortunately also are in the business of financing cars, and they are about to run out of money.

V. Alexander. The used car lots in his district are also selling new cars. Some of these dealers have formed a bank in his district and are paying 2½ per cent for money.

Martin states that he has just had a report from a source that has been reliable in the past, informing him that dealers are not selling used cars as rapidly as formerly, because they are holding prices high.

This source said used cars would move at lower prices.

Fleming believes that competent bank lenders are not lending on cars older than 1949 models.

Ringland. Used car dealers have had it easy. Maybe we are getting back to normal.

Martin thinks the probable trend in business may be moderately down. He cannot prove it statistically, but thinks this trend would be desirable based on a common sense analysis of the situation. On a common sense basis some downturn from these high peaks seems desirable. Very few companies today have executives who have had experience in anything other than a seller's market. In the modest decline of 1949, it seemed to him almost everyone ran to the Treasury for assistance. It might have been better at that time to have let the economy run down a little more, and we might then not have had quite as serious a situation as we had after Korea. Some downturn in business would probably be good for business now.

ITEMS II AND III

WHAT COMMENTS DOES THE COUNCIL HAVE TO MAKE WITH RESPECT TO (A) THE SYSTEM'S CREDIT POLICIES IN THE MONTHS AHEAD, AND (B) THE STEPS THAT MIGHT BE TAKEN IN THE FIELD OF CREDIT POLICY IN THE EVENT OF A CHANGE IN THE ECONOMIC CLIMATE?

IN VIEW OF THE CONTINUING DEMANDS FOR CREDIT ON ALL TYPES OF LENDERS AND THE PLANS OF BUSINESS FOR CONTINUED NEED FOR CREDIT, AND IN THE LIGHT OF THE TREASURY'S NEEDS NOT ONLY FOR REFUNDING BUT FOR NEW CASH DURING THE NEXT SIX MONTHS, AND WITH BANK DEPOSITS THROUGHOUT THE NATION CONSIDERABLY OFF DUE TO THE MILLS PLAN REQUIRING ACCELERATED TAX PAYMENTS BY CORPORATIONS, TOGETHER WITH THE HIGHER BILL RATE (MAKING IT LOOK LIKELY THAT BANK DEPOSITS WILL NOT RETURN IN APPRECIABLE VOLUME UNTIL LATE IN THE YEAR AND MANY CORPORATIONS MAY BE TEMPTED TO PLACE THEIR FUNDS IN TREASURY BILLS RATHER THAN DEPOSIT THEM IN THE BANKING SYSTEM) AND WITH SEASONAL LOANS RISING IN THE FALL, THE COUNCIL WOULD LIKE TO HAVE THE VIEWS OF THE BOARD AND OPEN MARKET COMMITTEE AS TO THEIR VIEWS ON EASING CREDIT CONDITIONS, ASSUMING THAT BANK LOANS WILL CONTINUE AT PRESENT LEVELS, DEPOSITS WILL NOT RETURN TO THE BANKING SYSTEM AS RAPIDLY AS HERETOFORE, AND SEASONAL LOANS WILL IN ALL PROBABILITY BE SUPERIMPOSED ON THE PRESENT HIGH LOAN LEVEL.

Brown reads Items 2 and 3 of the agenda and the conclusions of the Council, as expressed in the Confidential Memorandum to the Board attached. When the Council last met some members thought the money market should be tightened, but they now believe the situation is fundamentally different and the money market should be eased. Brown states that the members of the Council differ with Chairman Martin's statement in Boston that banks should anticipate their seasonal needs. At the time of the establishment of the Federal Reserve System, Brown believes it was understood that the System should provide funds for seasonal needs for banks. At that time wheat and cotton were more important relative to the whole economy than they are now. Soy beans, on the other hand, have become more important than they were at that time. There is also a tendency for heavier purchases now to take care of Christmas business. There have been changes over the years in the types of loans that make up the seasonal pattern of banks are to anticipate and take care of their own seasonal requirements, it may be necessary for them to sell short-term securities to obtain funds. The System or other banks must provide the funds. Eventually the System would probably be faced with the question of whether to provide funds through the open market or through rediscounting.

H. Alexander states that in February he was in favor of holding the money market tight, and he believes it was the proper policy at that time. The restrictive policy followed has become a very tight money policy now. He believes with Chairman Martin that some gentle turn down in the ecomony is desirable. However, he does not wish a decline that is too fast or too large. Some easing of the money market is desirable at present. Alexander hopes any downturn in the economy will be moderate.

Martin asks whether money in New York and Chicago is unavailable.

Brown. In Chicago money is very tight, and it is difficult to obtain.

H. Alexander. Money is not unavailable in New York, but the banks must squeeze something to get money for any loans. The market is very tight. The New York banks have lost deposits and their government bond accounts are down.

Brown gives illustrations of specific companies attempting to get loans and the difficulties which they are encountering.

Martin states that he asked the question to determine what the Council thought about the degree of tightness.

Fleming. Foreign governments and also American corporations are buying Treasury bills instead of leaving their deposits in the banks. Fleming believes that the Mills Plan is also causing some distortion in the seasonal pattern of loans and deposits.

Smith. Many of those with whom he has talked believe the money market is too tight and that there should be some easing of the market. Some of those who feel that the market is too tight state that a kind of "meat axe" control has been applied to the money market.

Ray. The country banks are complaining that the tightness of the market came too fast. They have seen their bond accounts fall. The psychological reaction has been unhealthy.

Brown. The Council has stressed that open market operations should apply only to short-term securities.

Martin. Is it fair to say that the Council suggests only a moderate easing of the money market and not a reversal of the interest rate situation? (A number of the Council members indicated their agreement with this view).

Fleming believes something must be done to hold the money market where it is now.

Davis. Money is not as tight in his district as in other districts. Many country banks hold long-term bonds and they complain if the prices drop. One United States Senator has told Davis that the tightening of the money market has gone too far.

V. Alexander. Cotton was at one time a seasonal business; now the cotton people borrow the year round.

Brown asks whether there is a Federal Reserve policy regarding borrowing by the member banks at the Federal Reserve banks.

Martin. The initiative for discounts rests with the local Federal Reserve banks, but is under the general supervision of the Board. If the discount rate is a penalty rate, then we have not had a penalty rate for a long time. In the process of freeing the market, we have not set up a set of rules. If the discount window is a right and not a privilege, then we should examine the rediscount rate more carefully than has been done.

Brown. The statement of Chairman Martin that the banks should anticipate their seasonal needs has upset the thinking of a number of banks.

Martin states it is a good idea to bring these matters up for discussion.

Ringland comments that a bank cannot always anticipate seasonal needs, and he describes a situation in which his bank could not anticipate seasonal needs.

Robertson replies that the views of Chairman Martin did not rule out taking care of a special situation such as Ringland describes.

Martin does not believe that it would be sound to have a condition in which banks gave no consideration to anticipating their seasonal needs.

Brown. If the bankers are to take care of their seasonal needs, they will have to sell government securities to the System or to other banks.

Robertson. If there is to be any easing in the money market, should it be through open market activities, through reducing reserves in the central reserve cities, or reducing reserves in all cities?

Brown states that the Council has commented on this matter in its answer, stating that temporary easing should be through open market operations. The Council has also stated that favorable consideration should be given to an early reduction in central reserve city reserve requirements. In the event of a business downturn, the System should ease the money market considerably by stepping up its purchases of short-term securities, and by reducing reserve requirements for all classes of banks.

ITEM IV

THE PROPOSAL IS BEING ADVANCED IN THE CONGRESS THAT THE RECONSTRUCTION FINANCE CORPORATION BE ABOLISHED AND THAT SOME ARRANGEMENT BE MADE THROUGH THE FEDERAL RESERVE BANKS OR OTHERWISE FOR THE EXTENSION OF LOANS, PARTICULARLY TO SMALL BUSINESS, WHICH WOULD NOT BE AVAILABLE THROUGH THE REGULAR BANKING CHANNELS. THE BOARD WOULD LIKE TO HAVE THE VIEWS OF THE COUNCIL ON THIS PROPOSAL AND, IF THOUGHT DESIRABLE, THE MANNER IN WHICH IT MIGHT BEST BE CARRIED OUT.

Brown reads Item 4 of the agenda and the conclusions of the Council, as expressed in the Confidential Memorandum to the Board attached. It would be unfortunate politically for the System if it had to administer an organization established to make loans to small business, or to extend credit for emergency, disaster, or defense purposes. There may be differing views in the Council on the question of whether to abolish the Reconstruction Finance Corporation, or to continue it and cut it down to size for such purposes as disaster or emergency or other types of loans, including those to small business.

Fleming. If an organization to extend small loans is ever connected with the Federal Reserve System, the political ramifications involving the System may be very great.

Wallace. On the matter of easing credit, the banking system should probably have a period to digest what has taken place in recent months in the interest trend and the money market. From the standpoint of the whole situation, it might be advisable notto eliminate the Reconstruction Finance Corporation at present.

Robertson. Does the Council feel the government should make loans to one small business to compete with another privately owned and financed small business?

Brown states he does not favor such loans.

V.Alexander. Whether we like the RFC or not, political pressures will be very strong for it.

Robertson. The Board cannot tell Congress that it does not favor an organization to extend loans to small business because of possible political pressures. What other reasons are there against the proposal?

Brown. The fundamental reason against the proposal is that the Federal Reserve System has a primary and more important function, which is monetary management. This function must not be confused or complicated by associating it with other functions.

Robertson. Then you state that any other agency should be set up separately and succeed or fall on its own and not be confused with the System's responsibility Is there a need for equity or debt capital for small business?

Brown states that it is not the business of government to provide equity or debt capital. Brown thinks the tax system now tends to prevent the growth of small business.

Martin reports that the comments of the Council have been very helpful.

H. Alexander states that he would like to add an additional comment regarding reserves. He believes that before going too far with open market operations, reserve requirements should be reduced. Alexander thinks that New York and Chicago especially need some relief. He would not be inclined to wait too long before reducing reserve requirements.

Ray agrees and can see no reason for central reserve city reserve requirements being higher than reserve cities.

Smith agrees.

Gund agrees.
(Other members of the Council agree).

H. Alexander. The occasion may be here soon for doing something about reserves.

The meeting adjourned at 12:35 P.M.

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The next meeting of the Council will be held September 13, 14 and 15, 1953.