A meeting of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System in Washington on Tuesday, December 15, 1959, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Hayes, Vice Chairman
Mr. Allen
Mr. Balderston
Mr. Deming
Mr. Erickson
Mr. Johns
Mr. King
Mr. Mills
Mr. Robertson
Mr. Shepardson
Mr. Szymczak

Messrs. Bopp, Bryan, Fulton, and Leedy, Alternate Members of the Federal Open Market Committee

Messrs. Leach, Irons, and Mangels, Presidents of the Federal Reserve Banks of Richmond, Dallas, and San Francisco, respectively

Mr. Riefler, Secretary
Mr. Sherman, Assistant Secretary
Mr. Kenyon, Assistant Secretary
Mr. Thomas, Economist
Messrs. Jones, Marget, Parsons, Roosa, Willis, and Young, Associate Economists
Mr. Rouse, Manager, System Open Market Account

Mr. Molony, Assistant to the Board of Governors
Mr. Koch, Associate Adviser, Division of Research and Statistics, Board of Governors
Mr. Keir, Chief, Government Finance Section, Division of Research and Statistics, Board of Governors
Mr. Knipe, Consultant to the Chairman, Board of Governors

Messrs. Hostetler, Daane, Baughman, Tow, and Wheeler, Vice Presidents of the Federal Reserve Banks of Cleveland, Richmond, Chicago, Kansas City, and San Francisco, respectively

Mr. Coldwell, Director of Research, Federal Reserve Bank of Dallas
Mr. Anderson, Economic Adviser, Federal Reserve Bank of Philadelphia
Mr. Holmes, Manager, Securities Department, Federal Reserve Bank of New York
Mr. Brandt, Economist, Federal Reserve Bank of Atlanta

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the Federal Open Market Committee held on November 24, 1959, were approved.

Before this meeting there had been distributed to the members of the Committee a report of open market operations covering the period November 24 through December 9, 1959, and a supplementary report covering the period December 10 through December 14, 1959. Copies of both reports have been placed in the files of the Committee.

Mr. Rouse called the Committee's attention to the result of yesterday's regular weekly Treasury bill auction, in which an average issuing rate of 4.535 per cent was established for the three-month bills and an average issuing rate of 4.833 per cent for the six-month bills. Dealer interest was reflected in awards of $337 million of the three-month bills and $231 million of the six-month bills. Rates established in the auction reflected a decline from the high rates established in the preceding week, and the fairly close range between the average issuing rate and the stop-out was indicative of a sounder position than in recent weeks.

Mr. Rouse went on to say that, as pointed up in the regular written report to the Committee, the period since the last meeting of the Federal Open Market Committee was an unusually difficult one for the Account Management. Normally, this period of the year is one where the Account is quite active in view of the seasonal pressures on member bank reserve positions and on the money markets. This year, open market operations over the past three weeks had supplied nearly half a billion dollars in reserves to the market, mainly through the outright purchases of Treasury bills. At the end of the period, however, the Account made a small volume of sales of securities to foreign accounts, thereby preventing additional funds from reaching a market that was already showing signs of ease. In view of easier reserve positions ahead, the Account successfully tendered in yesterday's Treasury bill auction to run off $123 million maturing Treasury bills. If reserve deficits should build up again, it would be an easy matter to reverse this through the purchase of Treasury bills in the open market, considering their current availability. Including yesterday's awards, and making no allowance for any net sales made yesterday, dealers held about $1.2 billion Treasury bills.

Operations were considerably complicated this year by the changes in Regulation D, permitting member banks to count part of their vault cash as required reserves. As a result of the uncertainty as to the distribution of these reserves and the extent to which they would find their way back promptly into the central money market, projections of bank reserve data were extremely difficult to interpret.

The Account Management therefore relied even more heavily than usual on the feel of the market as a guide to operations. Towards the end of the period, available data on country bank reserve positions seemed to indicate that the reserves released through the action on vault cash were working their way back into the money centers; reserve projections, therefore, seemed to have become more meaningful. The statistics, however, were still hard to interpret, and the Account Management would appreciate any comments from the Reserve Bank Presidents concerning their experience with member banks in their districts throughout the country.

As mentioned, the Account Management had been forced to rely to a large degree on the feel of the money market as a guide to operations, but interpretation of the signals given off by the market was by no means easy. While Treasury bill rates reached new high levels during the period, there were many occasions when the money market showed clear signs of easing. There was also evident in the market a growing uncertainty concerning the level of interest rates in early 1960, thereby bringing into sharper focus the important question of whether the usual easing of pressure on bank reserves and the money markets could be expected after the turn of the year, or whether the distortions in the seasonal pattern of credit demand due to the resumption of steel production might make for a shift away from the normal pattern of an easier situation early next year.

Uncertainty in the market concerning the trend of interest rates over the next month or so was reflected in the generally rising Treasury bill rates over most of the period. New high average issuing rates were established in the Treasury bill auctions on November 30 and December 7, and the higher Treasury bill rates spread to other short-term markets with bankers' acceptance rates, commercial paper rates, and finance company paper rates all moving higher. Towards the end of the period, with dividend and tax funds provided for, Treasury bill rates leveled off with the resumption of buying by some corporations, but the uncertainty about the longer-term trend of interest rates was still apparent in the market.

The upward pressure on short-term rates also affected the capital markets. Prices of Treasury notes and bonds generally moved lower over the period, although there was only moderate trading in this area of the Government securities market, most of it relating to tax switching. Much of the buoyancy also appeared to have gone out of the market for corporate and municipal securities. The stimulus that these markets received from the successful marketing of the American Telephone and Telegraph debentures now appeared to have worn off. Rates had edged upwards and most new issues had tended to move slowly out of dealers' portfolios. The largest issue scheduled for the period--the $100 million State of California issue--was postponed, since the State Treasurer felt that an anticipated rate of about 4 per cent was too high. The issue was now scheduled for January 13.

The bankers' acceptance market had also been under substantial pressure during the past few weeks. Seasonal increase in cotton bills and a growing volume of dollar exchange acceptances, some of them for Cuban and Brazilian account, had come into the market. At the same time, some banks had from time to time been selling acceptances in order to adjust their reserve positions. At the close of business yesterday, dealer portfolios had risen to about $48 million--an unusually high level--and $18 million in repurchase agreements was outstanding against bankers' acceptances.

As to the Treasury financing situation, Mr. Rouse stated that the Treasury had asked for consultations on December 29 and 30 concerning the raising of about $2-1/2 billion of new money in January and the method of taking care of the $2 billion issue of special Treasury bills maturing on January 15. At the time of original issue, it had been announced that the bills would be rolled over into 12-month Treasury bills. The Treasury was also arranging for advisory committees to be in Washington on January 27, 28, and 29 for discussion of the refunding of the February 15 maturity.

Mr. Rouse then turned to the matter of dealer positions. Ordinarily, he said, dealers build up inventories at this time of the year, in anticipation of some relaxation of pressures on bank reserves and the money market after the turn of the year, and the Account would normally give them some assistance in carrying these positions. The problem was whether, in view of projections which showed an easier position from now to the end of the year, the usual year-end support should be provided. In response to a question from Mr. Allen, Mr. Rouse stated that the projections of the New York Bank contained no allowance for the runoff of $123 million Treasury bills in yesterday's auction. He also said that he felt some help should be provided the dealers despite the low reserve figures, but that he would appreciate advice from the Committee on this point.

Thereupon, upon motion duly made and seconded, and by unanimous vote, the open market transactions during the period November 24 through December 14, 1959, were approved, ratified, and confirmed.

In supplementation of the staff memorandum distributed under date of December 11, 1959, Mr. Young presented a statement with respect to economic developments as follows:

Today's economic report is effectively summarized in four sentences. (1) Stability of wholesale price averages continues to contrast the middle phase of the present cyclical expansion with the middle phase of the 1954-57 cyclical upswing. (2) Recovery of industrial production from the steel strike setback is about as expected. (3) Recent balance-of-payments data confirm that our international position has not deteriorated further and probably has strengthened some. (4) Expansion of economic activity in industrial nations abroad continues to be vigorous.

Now for a brief run-down of recent domestic specifics:

(1) The November index of industrial production is estimated to be up one index point to 148 relative to 1947-49 as 100; the October index, it should be noted, was revised downward to 147 on the basis of information just available. With full-scale output in steel and steel-dependent industries restored in December, the December index should rebound by five or more index points. Indicative of prospects for industrial output in the months ahead is the auto industry's first-quarter assembly schedule at an 8 to 9 million car rate.

(2) At an outlook conference of homebuilders here in Washington last week, the consensus forecast was for 1,200,000 housing units in 1960. This was practically on the nose for the seasonally adjusted housing start rate for November which was released yesterday.

(3) Reflecting the acute shortage of new model autos, November dealer deliveries of domestic new cars fell to 374,000, or an annual rate of 4.6 million. This compares with an annual rate of 5.7 million as an average of preceding months. November used car sales were off a little from October, as were also used car prices, but both used car sales and prices were well ahead of a year ago.

(4) November retail sales were off one per cent from October, but only because of the sharp decline in automotive sales; in other lines, sales gains were widespread. In early December, department store sales were showing a continued small advance over November.

(5) Consumer instalment credit in October showed another $500 million increase, with over half of the rise in automobile credit.

(6) Sales and new orders in durable goods lines rose moderately in October and durable goods inventories declined substantially further to a level over $1 billion below end-of-July holdings. The October decline in total business inventories amounted to $500 million compared with a cutback of $300 million in September. While total business inventories may have declined somewhat further in November, they must surely be increasing again in December.

(7) Third-quarter business plant and equipment expenditures fell short of earlier projected targets according to the latest Commerce-SEC survey, and fourth-quarter prospects are also for a short fall below earlier projections. The total of such expenditures is still rising cyclically, however, and the most recent survey points to further rise through the first quarter.

(8) November employment rose moderately as the steel strike settlement returned workers to jobs on balance. The

employment rise was concentrated in durable goods industries; in nondurable lines, employment about held even.

(9) November hourly earnings of production workers in manufacturing were almost 3 per cent higher than a year ago. Weekly earnings were up very little, however. In the present economic cycle, manufacturing wage rates have not shown the tendency towards accelerating rise that they did through the comparable phase of the last cycle.

(10) With steel industry negotiations at a standstill, the Steelworkers Union has intensified bargaining efforts with other industries. Copper and can industry settlements provide for an 8 cent an hour wage increase for 2 and 3 years, respectively, plus fringe benefits worth more than 4 cents an hour per year.

Mr. Marget commented as follows with respect to the United States balance of payments:

When I last reported to the Committee, I suggested that there are two types of error against which we should be on our guard, so far as developments with respect to our balance of payments are concerned. "One is the error of supposing that no adjustment is taking place in our balance of payments; the other is the error of supposing that the adjustment is taking place so rapidly and certainly that we no longer have a balance-of-payments problem, and that we therefore have no need to frame our policies with reference to what is happening in that area." I am still very firmly of the view that both of these errors are to be avoided. If, this morning, I stress particularly the desirability of avoiding the second error--which, for brevity, I shall call the danger of excessive optimism--it is precisely because the latest news that we have with respect to balance-of-payments developments is, as far as it goes, encouraging.

You may recall my pointing out, last time, that the evidence that we thought we had with respect to the improvement of the trade picture in the third quarter of this year was not being reflected in the figures for our over-all deficit in the third quarter as measured by the total gold and dollar outflow. Fortunately, the September trade figures that I reported last time were encouraging, in that they continued to give evidence of the pick-up in foreign demand for our exports which has been apparent since June of this year, so that the explanation of the maintenance of a gold and dollar outflow at an annual rate as high as $4 billion--

which was also the rate for the second quarter--had to be sought in some of the nontrade items, such as capital movements and aid transactions. Nevertheless, one would have felt much more comfortable if the improvement in our trade picture had been more clearly reflected in the figure for the over-all deficit in terms of the total international movement of gold and dollars.

From this standpoint, it is of considerable interest to see what is shown by figures for gold and dollar movements in October, which were not available when I made my last report to the Committee. Instead of showing the kind of steady increase in foreign and international gold and dollar holdings resulting from transactions with the United States which has been the source of our concern for so many months now, these foreign and international holdings actually declined in October by $159 million. October, indeed, was the first month in about two years to show a substantial decline in foreign holdings of gold and dollars. It is true that this figure includes the repayment of $250 million by the United Kingdom to the Export-Import Bank, but it is also true that, even excluding this payment, net transfers to foreigners in October were less than one-third of the monthly average for the last 1-1/2 years.

Unfortunately, the November figures on foreign accounts with commercial banks are not yet available. December transfers of gold and dollars to foreigners, however, are always small, owing largely to the receipt of year-end payments on our postwar loans to the United Kingdom and France. If the November market figures should turn out to have been as favorable as those for October, net transfers for the current quarter would probably be negligible, and total transfers for the calendar year 1959 might even fall below last year's total of $3.4 billion. This would, of course, be a much better result than the total of $4.5 billion which was forecast by the group that met a few months ago under the auspices of the National Foreign Trade Council, and better even than the total of $4 billion which has figured in most of the more recent forecasts.

Moreover, the trade figures continue to show the kind of steady, if slow, improvement for which we have been hoping. There has, in fact, been a general leveling off in our imports after May-June, and this leveling off has been reflected in some of the areas--such as automobiles and steel--in which doubt has been expressed as to our ability to maintain our competitive position. Similarly with exports. In September and October they ran at a seasonally adjusted annual rate some

11 per cent above their February-April low (a rate of expansion considerably faster than that experienced during the previous cyclical upswing in exports in 1953-54), and they also included increases in areas in which doubt has been expressed about our competitiveness. There were increases of more than 20 per cent, for example, in exports of autos and trucks, textile manufactures, and agricultural products, while exports of machinery and of chemicals also rose by more than 10 per cent.

This is certainly encouraging news, as far as it goes. It does mean that the processes of adjustment in the international accounts seem to be working, as we said they would work if the right policies were followed. That, after all, is the key proviso. At the moment, the outlook is for the kind of expansionist pressure in the economies of our trading partners which will facilitate further adjustment if we succeed in keeping comparable pressures from getting out of bounds in our own economy. There is plenty of room for a reasoned optimism that our international accounts can be brought into closer balance, on the assumption that we follow policies calculated to bring about that result; there is no room for a fatuous complacency that would expect this result to come about in any case, regardless of the degree of fiscal and monetary responsibility that we choose to show in dealing with the problems that face us.

Mr. Thomas made the following statement concerning financial developments:

As was to be expected, interest rates rose in the latter part of November and early December. Short and medium rates generally went above the high levels reached in September, but some of the long-term rates have not reached their September levels. Yields on outstanding corporate bonds, which had not participated in the October and November decline, have not increased particularly, and averages for State and local government bonds have also not risen, although they had declined substantially since September. New issues of corporate bonds, however, have been sold at higher rates. Some municipal offerings have moved fairly slowly and amounts available for sale have increased. Within the past week, interest rates, particularly short-term rates, have shown some tendency to level out.

Some rise in interest rates, particularly at short-term, was to be expected at this time because of the pressures of seasonal liquidity needs. The large corporate and other non-bank holdings of short-term Government securities and other paper, held in lieu of cash balances, means that pressures develop in these markets whenever cash needs mount. Such needs are always temporarily large in December. It is likely also that the rapid expansion of steel operations in the past few weeks has created some additional credit demands, following the comparative lull during the fall months. Another factor of uncertain magnitude given prominence in market discussion is the anticipation of a renewed cyclical rise in interest rates during 1960 in view of the expected high level of economic activity. Stock prices, after moving within a narrow range for three months, have risen in the past three weeks to near the highs reached last summer.

System operations have been a moderating factor in interest rate movements as reserves have been supplied in adequate amount to meet customary seasonal needs. The steadier tone in the money market in the past week may reflect the satisfaction of current liquidity needs, aided in part by System actions.

In the next few weeks there will be cross currents in the factors affecting the money market and the course of interest rates. Seasonal relaxation of pressures is to be expected. As in July and October, the passing of the seasonal cash needs should bring to an end the temporary rise in rates, and may already have done so. Short-term interest rates nearly always decline in January after rising in December. A factor of easing this year not present in other recent years is the redemption of a December tax bill, which will reduce the need for corporations to raise funds to meet taxes or for other purposes.

This latter influence, however, will be offset in January, and perhaps earlier in anticipation, by new cash borrowing by the Treasury. At least $1.5 billion will need to be raised early in January (presumably through the sale of additional June tax bills) and more cash will have to be obtained later in the month. These operations, and also refunding of the quarterly special bills maturing January 15 and of the very large February certificate maturity, will tend to keep the market in a state of uncertainty for the next two months. Other credit demands--from business for inventory build-up and gradually for increased capital expenditures, and from consumers to finance mounting automobile purchases, as well as the continued strong demands for mortgage financing and from State and local governments--may be large in the aggregate. Expanding economic activity and rising interest rates in foreign money markets may also be an influence toward high rates in this country now that freer movement of liquid funds between such markets is feasible.

Over an extended period of time, current savings, stimulated by prevailing high interest rates, may prove adequate to meet the credit demands. Substantial retirement of Federal debt that begins in March should release funds for other uses. Whether or not borrowing demands are likely to be so concentrated into the next three months as to exceed the available supply of lendable funds and cause further increases in interest rates remains to be seen. Should they do so, there would also be pressures on other resources and tendencies toward rising commodity prices. Little can be gained by attempts to supply funds to keep interest rates from rising under such circumstances. There is a possibility, however, and perhaps even a likelihood, that credit markets may be well balanced in the months ahead and that interest rates may now show further increases.

Currently, credit demands have not been excessive in the aggregate. New capital issues by corporations and by State and local governments were in moderate volume in November and are continuing moderate in December. Total loans and investments of commercial banks actually declined in November. This is an unusual development and is due in part to absence of Treasury cash financing in that month. Yet, when partly estimated figures for city banks for the next two weeks, which include Treasury financing, are added, the totals are still moderate. In the six weeks, total loans at city banks increased less than usual, while business loans increased by close to the usual seasonal amount. Holdings of securities showed a net decline for the period. Country banks likewise showed little change in total loans and investments during November, although increases have occurred in most previous years.

The money supply, after declining for three months, showed a slightly greater than seasonal increase in November, but the further rise at city banks in the first two weeks of December was much smaller than usual. Time deposits declined, as is usual in November. U. S. Government deposits also declined. However, nonbank holdings of liquid assets in the form of Government securities increased further as banks reduced their holdings. Turnover of demand deposits outside financial centers, which like the volume of deposits had been relatively steady since last spring, increased in November. Although the money supply is only about 1 per cent higher than a year ago, turnover for the past three months has averaged about 7 per cent more than in the same period last year.

Reserves have been supplied to meet customary seasonal needs for currency and credit during recent weeks in part through System purchases of securities and acceptances and in part through the release of vault cash and the new allowance for remittance drafts. The actual amount supplied through releasing vault cash will not be known until reports are received from member banks for the reserve periods. The reaction of the banks to such a source of funds can be detected only from market action. It would appear, as Mr. Rouse has pointed out, that utilization of the existing reserves, while slow at first, has been felt at least to some extent in the market.

Currency demands, which conformed closely to the usual seasonal pattern in November, appear to have shown a larger than usual increase in the first half of December. Required reserves, on the other hand, have shown a somewhat smaller than seasonal increase, owing in large part to allowance for remittance drafts. Current estimates of required reserves, however, are still preliminary and subject to revision.

In the next two months, Federal Reserve operations will be primarily concerned with the large scale money market adjustments characteristic of the season. It will also be necessary to maintain conditions that will not interfere unduly with the series of Treasury financing operations. This does not mean, of course, that special efforts should be undertaken to protect Treasury financing from the effects of competing credit demands. The course of these other demands will need to be watched carefully.

Seasonal reserve needs appear to have been fully met by operations to date. Further needs may be covered by the usual large mid-December float increase now due to begin. From now on, System operations will need to be directed toward absorbing reserves, although action can be gradual and moderate, as liquidity needs normally continue large during the last half of December. In the first three weeks of January the System portfolio would have to be reduced by nearly $1 billion if net borrowed reserves are restored to the $500 million level.

In January, the System should begin to be alert to developments in the private credit area. In view of the prospects for a high level of economic activity in the months ahead, strong and vigorous monetary and credit demands may soon become evident. A considerable flow of funds can be effected through the shifting of nonbank holdings of short-term securities. Banks, moreover, under the pressure of demands from customers, may be willing to increase their borrowings to obtain needed reserves. These sources of funds provide cushions that could mitigate the restraining effects of any restrictive policies the System may want to adopt. Under all the circumstances, there seems to be greater danger in too little, rather than in too much, restraint.

Mr. Hayes presented the following statement of his views with respect to the business outlook and credit policy:

In my judgment the Committee faces difficult decisions today and early next year, despite the fact that there have been no startling recent developments and that the business outlook is rather satisfactory. Essentially the problem we must resolve is whether we are in danger of exerting too restrictive an influence on credit and the money supply in view of the extent of existing unused resources in the economy and the need to encourage further gradual expansion.

First, as to the business situation: Most general business indicators seem likely to reach or exceed previous records in the near future. Consumer buying is being supported by a growth rate for consumer credit which may, if it persists for many months, bring a need for re-examination of the whole area of selective consumer credit control. On the other hand, housing construction is declining nationally (although not in our District), and there is as yet no evidence of a general scramble for inventories. The latest SEC estimates on plant and equipment expenditures suggest less of an uptrend than had been expected earlier. Granted that the most recent survey of appropriations suggests the possibility of substantially larger capital spending ahead, it may be significant that margins between capacity and output are now considerably wider than in 1955.

The price situation still exhibits a divergence between the movement of wholesale and consumer prices. There is indeed cause for concern in the inexorable rise in the price of services, in the cost-push implications of many recent wage settlements, and in the possible upward pull on prices exerted by the business boom in Europe. On the other hand, current prices in general do not reveal any great upward pressure. Longer-range concern over inflationary threats may well be partly responsible, together, of course, with business optimism, for the persistent recent gains in stock prices, and it would be highly regrettable if these fears should undermine such improvement as we have seen in the last few months in foreign confidence in the dollar.

Since the last meeting the rebound in business loans from the October lull seems to have become more pronounced. There is widespread expectation of greater-than-seasonal loan demand early next year, as the effects of the steel strike wear off. Bank liquidation of Government and other securities was heavy in November, causing a drop in total loans and investments in contrast with increases in 1955, 1956, and 1958. At the same time, loan-deposit ratios reached new highs both in and outside of New York.

Treasury financing operations, both past and prospective, have had much to do with the uneasy state of the money and capital markets in the past three weeks. Commencing with the expected announcement of a cash offering around the end of this month, the System will be confronted with almost continuous Treasury operations through most of January and February.

In deciding on credit policy at this time, I think we must recognize that the economy is still operating well below capacity without any strong upward price pressures from the demand side and that further sound business expansion is much to be desired. Frankly, I am wondering whether the level of interest rates attained at the peak last week would, if sustained, be appropriate and healthy at this stage of the expansion. It is true that the rate bulge was due in large part to seasonal pressures and Treasury activities, but there is apprehension in the market that the usual January relief from money-market pressures may not occur this year. On this point we can only await developments. But I can see some risk that the cumulative effects of the tight check on the growth of the money supply and the low liquidity of the banks may unnecessarily impede the current economic expansion.

Under these circumstances we should certainly avoid any further tightening of credit, and, while the present general degree of restraint should be maintained, any doubts arising from day to day should be resolved on the side of ease. With statistics on net borrowed reserves still perhaps somewhat less meaningful than usual, in view of the new vault cash provisions, I think the "feel" of the market should be the principal guide for the Manager, and I think he should have ample leeway at this period of seasonal pressures and uncertainties as to the pattern of credit demands resulting from the strike. It seems to me that the Committee might well focus its attention on the level of market rates and consider whether the recent peak rates, if they should recur and persist, might suggest undue and undesirable pressures. The behavior of member bank borrowing over the next few weeks should also provide a useful measure of such pressures.

I would think it quite unwise to consider any change in the discount rate at this time, for we should be reluctant to validate the recent rate bulge to the extent that it may have reflected purely temporary pressures--and with respect to more lasting pressures, I think we should move cautiously and review the whole picture early next year. Even if a discount rate increase should then seem desirable, as a practical matter action might have to be deferred until completion of the Treasury's January and February financing. Incidentally, a case might be made for delaying the date of the next Committee meeting until January 12, in view of the fact that by January 5 the market will have had hardly any time to evaluate credit and capital pressures following the year end and the long New Year's week end.

As for the directive, I would like to find a way at the year end to show that we are concerned over whether the cumulative effects of continued restraint may have become sufficient for a time. I hope we will find that we can, gingerly and without undue risk on the price front, permit some further growth in the money supply over the period ahead, when the usual seasonal loan contraction may be partly offset by reviving credit demands as the effects of steel stagnation wear off. But I have not been able to find suitable wording for all of this, and would be inclined to leave the directive as it is, though I am not unsympathetic with the suggestion as to wording offered by Mr. Mills at the last two meetings.

Mr. Erickson said that the New England industrial production index, which remained fairly constant during July, August, and September, dropped three points in October. The November survey of New England purchasing agents showed that 52 per cent expected no substantial change in production, while 35 per cent expected an increase and 13 per cent a reduction. The 13 per cent compared with 18 per cent the previous month, while the 35 per cent compared with 43 per cent in October and 51 per cent in August. The Dodge reports showed a 4 per cent drop in construction contracts in October, the fourth consecutive month that a decrease was reported. For the first ten months of this year, there was an increase of two per cent compared with last year, the increase being less than the national average. Residential construction had been slipping in recent months, but for the year the figure was still 21 per cent ahead of the preceding year, this gain being slightly higher than the national average. Employment was up two per cent compared with the previous year, not as much as nationally. Electrical machinery, including electronics, was the fastest growing industry in the district from the standpoint of employment, while no gains were found in primary metals, foods, transportation, or public utilities. Department store sales were below the national average; however, the 11 days after Thanksgiving showed a better sales picture than the similar period a year ago. District banks reporting Federal funds transactions were net sellers through November, but they had been net buyers since the first of December. There had been more active use of the discount window during the past three weeks than during the previous six or nine weeks. Last Friday was the largest day in some time, due primarily to borrowing by Boston banks.

Mr. Erickson said that he would suggest no change in the discount rate or in the directive. With regard to open market operations, he felt that the Desk had done a good job in the past three weeks, considering all of the factors with which the Desk had to contend. Recognizing those factors, he would recommend that the Account Manager be given considerable latitude to maintain the same degree of restraint, without tightening at all.

Mr. Irons reported that Eleventh District activity was at a high but relatively stable level. During the past few weeks there had been some increase in strength, but nothing sensational. Crude oil production and refining were up somewhat, along with department store sales, while employment had improved seasonally. Estimates placed cash farm income for this year at about last year's figure, which meant a lower net income due to the increased cost of doing business. The construction picture showed some improvement, with an increase in nonresidential construction offsetting a slight decline in residential construction. District banks did not appear to be experiencing the seasonal deposit increase that would normally be expected during the fourth quarter of the year. In fact, deposits of weekly reporting banks had held steady for most of the year. Loan totals also were quite stable, with no significant increase in the past few weeks. There had been no substantial increase in borrowing at the Reserve Bank, but there was rather substantial use of Federal funds on the part of some of the larger city banks; in contrast with the banks in Houston and San Antonio, those in the Dallas area were rather steady net buyers of Federal funds. On the whole, the Eleventh District situation was one of high-level activity, without substantial change in either direction. While attitudes were generally optimistic, there was a considerable degree of uncertainty reflecting questions such as those with respect to the steel negotiations, the rapidity of further upward movement in business activity, interest rate levels, and Treasury problems during January and February.

Mr. Irons said that he would not favor a change in the discount rate or in the policy directive at this time. As to open market operations, he realized that the past three weeks had been difficult, particularly with the vault cash action added to other factors that were in the picture. He would like to see about the same degree of restraint maintained that had been achieved prior to the past three weeks, when signs of easing began to appear at times. While this was understandable in the circumstances, he felt that the deviations had tended to be on the side of ease rather than restraint, and he would be cautious about deviating in that direction. Instead, he would try to maintain a firm restraint in the market, and possibly even deviate on the side of firmness rather than run the risk of creating ease at this time. While he would hope that deviations could be avoided, he realized that that was probably not possible. The statistics might not always be too meaningful, and the people on the firing line must have considerable leeway in maintaining a situation consistent with what the Committee talked about in a general way.

Mr. Irons said he would feel that, as Mr. Hayes had suggested, there might be merit in holding the next Committee meeting on January 12, 1960, rather than January 5; the earlier date would provide only a short interval following the Holiday Season and the long New Year week end.

Mr. Mangels said that the resumption of steel production had generated some improvement in the Twelfth District in early December. Otherwise, the changes that were evident arose primarily from seasonal factors. There had been some increase in the demand for lumber to build up wholesale and retail inventories. As a consequence, lumber prices firmed; plywood rose from $64 to $68 a thousand, thus providing some margin for producers. Announcement last week by three savings and loan associations in the San Francisco area that, effective January 1, 1960, they would increase their dividend rate from 4 per cent to 4-1/2 per cent had resulted in considerable publicity on the radio and in the press. The banks were asked whether they would seek an increase in the maximum rate payable on savings deposits, and savings and loan sources had been saying in their own meetings that they hoped to get a substantial amount of funds to enable them to expand their real estate loans rather extensively. The banks estimated that, after interest credits were given at year end, they might lose

10 per cent of their time deposits, which would be quite a substantial factor and would require a period of adjustment. The money might not come back, and in any event there would be a period when the funds were out of the banking system.

While there had been some decrease in the level of net borrowed reserves, Mr. Mangels felt that the statistics tended to understate the degree of tightness in the market. In his view the market had been tightening quite substantially during the past couple of weeks. Thus far the vault cash action apparently had not aided a great deal. In the Twelfth District only 40 of 200 banks had benefited, and in no case was the amount of benefit substantial. While the System should be careful to maintain sufficient restraint to avoid serious inflationary pressures, he felt it should also be careful--perhaps more so--to avoid undue tightness that might have an adverse effect on general business conditions. Already, he noted, there were a number of reports from banks that they were calling loans in rather substantial amounts, and this might ultimately have harmful effects. Therefore, without changing the directive and without any general change in policy, he would give consideration to operating during the forthcoming period with less restraint than had prevailed during the past three weeks. As to the discount rate, he noted that the current level of bill rates was causing some speculation as to whether a change was imminent. While he did not think that a change should be made now, he felt that the matter deserved some consideration at a time when the System had a green light.

Mr. Deming, who participated in the morning telephone calls during the past three weeks, commented that he had built up much sympathy for the Desk in the light of the difficult statistical situation that prevailed. Turning to the Ninth District, he said that trends, relative to national trends, in the past several weeks had continued to reflect the lesser gains in the district, a situation which he believed would continue for the next few months. Perhaps the best single indicator presently available for the district was nonagricultural employment, which in October was only slightly (0.3 per cent) ahead of a year ago in contrast to a 2.4 per cent gain for the national series. The Reserve Bank had been working on the development of personal income data but so far only had figures for Minnesota. On a seasonally adjusted basis, total personal income in that State in October was $200 million below the June and July highs, representing a drop of 3 per cent. Banking data showed about the same picture and also demonstrated some liquidity loss and money tightness. Total deposits at the close of November were off appreciably from a year earlier, with much of the loss concentrated in the past few weeks. At the same time, total loans were up strongly; total investments were down by four-fifths of the loan rise. The vault cash release meant little to district banking, with only $3 million in reserves added by this action. About 25 per cent of the country banks were affected, mainly in the northern mining areas. A check of Treasury bill tenders before and after the release showed no appreciable change in amounts tendered for by banks that had received some benefit from the vault cash release. What had happened to correspondent bank balances was not known as yet, but conversations with city bankers indicated that they saw no inflow of funds.

With respect to the iron ore situation, Mr. Deming commented that warmer weather in December had helped the shipping picture and that it now looked as though a total of 42 to 43 million tons of ore would be shipped from the Lake Superior region this season. While somewhat better than the estimate a month ago, this would be 20 per cent less than last year's poor record. More importantly from a national standpoint, however, analysis of stocks and shipments from all sources now indicated that ore supplies should not bottleneck steel production, although the margin might be thin by next April and might be thinner at interior steel plants than at those in Pittsburgh and more easterly points. It was understood that the American Iron Ore Association, which had been somewhat more pessimistic concerning ore shipments, was revising its estimates upward.

With regard to the national scene, Mr. Deming said that the statistics and tone pointed to a vigorous upswing from the strike-induced lows in activity. However, he continued to be concerned about the unemployment figures, particularly those relating to long-term unemployment, and also about the data on the money supply and liquidity. These seemed to him to indicate less danger of unsustainable expansion and more danger that too tight a monetary policy could inhibit real growth. Accordingly, he would not like to see any further tightening. He would prefer to have errors made--if they had to be made--on the side of ease, and he would not object to backing away mildly from the existing degree of pressure. He was not quite sure how to measure the level of pressure at this time but was inclined to agree with Mr. Hayes that perhaps interest rates could afford a better guide at present than they might at some other time. Mr. Deming felt that the wording for the policy directive suggested by Mr. Mills at the last two meetings perhaps represented more nearly what the Committee was doing at this time than the present directive. However, he was not sure that he would want to make enough change in policy to warrant a change in the directive.

Mr. Allen made substantially the following comments with respect to Seventh District developments:

> From the viewpoint of industry, the business outlook in the Seventh District continues highly optimistic.
>
> First, as has been said, national surveys indicate a 1960 increase in almost all types of capital spending. The Seventh District produces at least one-third of the nation's capital goods. Our contacts in that area support the expectation that these industries will be booming in the coming year, with present order backlogs no worse than good in any category and excellent in many. There is one exception--petroleum refining--which is unlikely to increase capital expenditures in 1960.

Employment prospects in industry, therefore, appear bright for early 1960. Although secondary layoffs are still occurring in steel-using industries, recalls are outnumbering new layoffs. Automobile production will step up rapidly now that all assembly plants, effective with the middle of this week, will be rolling. A record number of passenger cars are scheduled for assembly in the first quarter of 1960, which should restore conditions of fairly full employment even in our hardest hit cities, Detroit and Flint.

Our farmers have less reason to be pleased with the outlook. The parity ratio for agricultural commodities in November fell to 77, the lowest level since before World War II. Average prices for agricultural commodities dropped 2 per cent in the month ending November 15 and were 7 per cent below a year earlier. Prices paid by farmers were slightly above the preceding month. Corn picking in Iowa, and in localized areas elsewhere in the District, has been hampered by bad weather, and there is still 10 to 15 per cent of the crop to be picked, compared with an average of 5 per cent at this date in previous years.

Our financial economists, and our bankers too, expect higher interest rates in the next few months. They point to a probable need for funds to carry higher business inventories and receivables and to the forthcoming requirements of the Treasury, refundings and otherwise. Loans of our larger banks are beginning to reflect the pre-Christmas and corporate tax-and-dividend-period credit demands, but so far the expansion at our weekly reporting banks has been mild compared both with a year ago and with banks in other parts of the country. One factor is that metals industries have continued to reduce borrowings. But our bankers expect business loans to increase in the next two weeks.

Reserve pressures have shifted unevenly but on the whole appear to have been somewhat less severe in the Seventh District than elsewhere. The uncertain effects of the new vault cash rule make the situation somewhat hard to evaluate. Our data indicates that the newly created reserves will go primarily to banks in industrialized areas.

Eighty per cent of the reserve-eligible cash is in banks in metropolitan areas, half of this in urban centers of Michigan, a relatively highly industrialized State. The prevalence of branch banking in Michigan is also a factor. In number, more than 70 per cent of the District's central reserve and reserve city banks have reserve-eligible cash, as against only 35 per cent of our country banks.

Mr. Allen considered the outlook so obscure that the System must wait on the discount rate even though it was out of line with other money rates. However, he felt the discount rate must be given serious thought in January. While he would not mind changing to the phraseology suggested by Mr. Mills for the directive, he would prefer to do nothing at this time. On the general picture, he found himself in agreement with the comment of Mr. Thomas that the greater danger was in too little rather than too much restraint. Therefore, he was also in agreement with what Mr. Irons had said. He would neither propose nor favor deviations on the side of ease. Instead, he would try to stay just about as at present and hope for a clearer picture by the time of the next Committee meeting.

Mr. Leedy said that Tenth District conditions had not changed materially in the past three weeks, although there had been some improvement in the employment situation since the end of the steel strike. The three General Motors assembly plants in the Kansas City area had recalled all of their furloughed workers and had indicated that they might employ additional workers before the end of the year. Loan expansion continued at district weekly reporting banks, with expansion of credit to finance retail trade one of the most notable developments in business loan demand this year. The increase in this type of loan at reporting banks through November was roughly $35 million, whereas the largest previous increase, in 1955, was in the neighborhood of $21 million for the full year. Judging from department store data, the increased percentage of sales on an instalment basis had apparently been a factor, along with expansion of sales, in increasing the demands of retailers for credit. With the yield on Treasury bills having risen sharply above the Federal funds rate, a few larger banks in the district that customarily sell Federal funds were diverting part of their excess reserves to the bill market.

As to policy, Mr. Leedy said that the distortions due to the end-of-year situation and the imminence of Treasury financing operations suggested to him doing nothing more than the System had been doing. Accordingly, he aligned himself with those who felt that it would be advisable to continue the degree of restraint at which the Committee had been aiming, but which may not have been fully accomplished in the past few weeks. He agreed with the view that errors on the side of ease should be avoided. Except for the end-of-year period and the uncertainty with respect to the steel negotiations, he felt that the Committee ought to be thinking of increasing restraint as well as moving on the discount rate. It seemed to him there was such strength evident in the economy and in the projections for next year that the System need not be too much concerned about the possibility that it was dealing with a delicate situation which might be triggered adversely by firm and positive action. Even if the System should overshoot the mark, he did not believe that would seriously impair the developing expansion that seemed to be under way. This view, he felt, was reenforced by the public psychology that seemed to exist on every hand. In summary, his recommendation would be to continue until the next Committee meeting the same degree of pressure that the Committee had intended to apply in recent weeks.

Mr. Leach commented as follows with respect to Fifth District developments:

> Following a high-level plateau, Fifth District industry and trade have apparently renewed their upward movement. The Southern Furniture Market was reported to be extremely good, with the placement of forward orders continuing to build up an already substantial backlog which currently exceeds last year by about 50 per cent. Textiles continue in their most favorable position in recent years with forward buying carrying into the fourth quarter of 1960 and mill inventories very low. Bituminous coal production has increased appreciably since the resumption of steel output. A considerable amount of construction of new commercial facilities in progress and planned promises a supply of new opportunities in the months ahead. Indications within the District point to increasing employment, income, and spending, a continuing strong demand for major Fifth District products, and added impetus for production from abnormally low inventories.
>
> The outlook for farmers is less favorable. The level of agricultural income is sharply down relative to 1958, which was an unusually good year. Through December 4, gross returns on flue-cured tobacco, our largest money crop, are down about 3 per cent from the similar period last year.
>
> Pressures on District banks have been heavy since our last meeting. Average daily borrowings from the Federal Reserve Bank of Richmond since the first of December have been higher than in any similar period in the last six years.

As to policy, Mr. Leach noted that there was now an open period in the Treasury financing schedule and that the discount rate was somewhat out of line with other short-term rates, especially the 90-day bill rate. He recalled, however, that Treasury bill rates usually peak seasonally about this time in December and then decline. Under present circumstances, it seemed to him that System policy should be one of continuing to hold a tight rein, pending developments, rather than to pull the reins even tighter or move in the direction of ease. While he rather liked the wording for the directive that Mr. Mills had proposed at the two most recent Committee meetings, he did not think it was a good time to make any change in the directive which would suggest a change in policy. If there was to be no change in policy, he would not change the directive. In summary, he would not favor a change in the directive, in the discount rate, or in the degree of pressure now exerted by open market operations.

Mr. Mills said he wished to return to his plea for a System monetary policy of moderate restraint over the expansion of bank credit as compared to a policy of relatively severe restriction. In that connection, he believed that the mechanical aspects of System policy operations in recent weeks, as measured by the level of negative free reserves, had been in the right direction and were appropriate to the economic circumstances portrayed to the Committee by Messrs. Young, Marget, and Thomas. Moving into a new year, he saw a need to look further afield than the next meeting of the Committee and to probe into the relatively obscure economic future. Accordingly, he presented the following statement:

In developing Federal Reserve System monetary and credit policy for 1960, in my opinion, the Open Market Committee would be well advised to reset the theme in which policy is formulated. Price inflation and interest rates have been the financial problems with which the System has treated for several years past. However, in retrospect these problems are symptoms, rather than the cause, of the basic difficulty that must be dealt with, and which is credit inflation. Although the term "credit inflation" has gone out of fashion, the fact that a vast credit inflation exists must be reckoned with. The present period of credit inflation can be traced back to the lifting of the World War II economic controls which was followed by a rapid and continuous inflation of private credit and an almost equally rapid inflation of public credit, both of which have carried on through 1959. A doubling of national productive capacity, a rising standard of living, and a far-reaching foreign aid program have all been accomplished within the context of a credit inflation which may now be entering a critical phase in which Federal Reserve System monetary and credit policy may well become the deciding factor as to whether the tangible economic gains of recent years will be preserved or lost.

At this crucial time, when the burden of public and private debt and the illiquidity of the commercial banking system are matters for serious concern, painstaking judgments must be reached as to how Federal Reserve System monetary and credit policy can be made to contribute to national economic development in ways that will see a digestion and consolidation of outstanding debt to a degree that will lay a secure foundation for an inflation-free renewal of credit expansion. An alarmist view of the seriousness of the present credit inflation and the adoption of a counteroffensive policy of severe credit restriction might be expected to so choke off the availability of credit as to halt economic growth in its tracks and induce deflation. A more realistic policy would be one of reasonable restraint over the expansion of credit that would permit that measure of credit expansion that is consistent with

> real growth in the gross national product at the same time that accumulated incomes are largely diverted toward the repayment of debt rather than toward expansive expenditures involving the additive of newly created credit. In my belief, Federal Reserve System monetary and credit policy for the foreseeable future should aim at moderate restraint over the expansion of credit.

Mr. Mills said that he would not favor an increase in the discount rate. He wished to propose again to the Committee a change in the directive so that clause (b) would read "to fostering sustainable economic growth and expanding employment opportunities while guarding against inflationary credit expansion."

With respect to the question raised by Mr. Rouse regarding dealer positions, Mr. Mills said it would seem that the Desk could give reasonable help to the dealers and the market in the latter days of this month, but on a reluctant basis and bewaring of "crocodile tears."

Mr. Robertson said he found himself in almost complete agreement with Messrs. Irons, Allen, Leedy, and Leach. It seemed to him the strength of the economy was such that one could not afford to be easing off at this time. Instead, he felt that this was a time to be holding steady, notwithstanding the fact that this might result in problems for the System during the Treasury financing period in January. By holding steady he did not mean making all of the errors on the side of ease. During his tenure as a member of the Committee, he felt that it had usually been the tendency to lean toward ease when the Committee wanted to hold a steady course. Therefore, he would suggest that errors be on the side of restraint in the hope of maintaining an even keel. In saying this, he did not mean to criticize the operations of the Desk during the past three weeks; this had been a difficult time with the vault cash release added to other factors. Nevertheless, he felt that it had been more customary to veer on the side of ease rather than restrictiveness, and he could see no justification in easing at this time. If anything, he felt that the Committee ought to be pushing as hard as it could to hold a steady, firm rein. The policy that the System had been following appeared to be beginning to bite, and it should, perhaps a little more severely, if the System was going to curtail what he thought was in the offing, namely, boom conditions. He would not favor a change in the directive. A case could be made for increasing the discount rate, but it was not a sufficiently good case to cause him to urge an increase.

Mr. Shepardson said he could not add much to what Mr. Robertson had said. The end-of-year situation, the easing that normally follows after the first of the year, and the fact that Treasury financing was to be in the picture a good part of the next two months all tended to make it difficult to take a tighter hold at this time. However, since he foresaw a burgeoning of activity after the turn of the year, he felt that the System should maintain as firm a grip on the situation as possible. Because of the inadvertent but apparently inevitable slippage when attempting to maintain the prevailing degree of restraint, he would suggest, like Governor Robertson, that any errors be on the side of restraint. With reference to the point mentioned by Mr. Mills, he felt that all should be somewhat concerned about the extent of credit expansion. As he saw it, the best way of meeting the problem would be to maintain the existing degree of restraint. Since the System probably would want to go farther rather than turn back if things picked up after the turn of the year, and since the System might be retarded in facing that situation because of Treasury financing activities, it seemed to him necessary to maintain as tight a position as possible at the moment. In summary, he would recommend no change in policy or in the discount rate, and he would like to maintain the full degree of market restraint that now existed.

Mr. King said he felt that System monetary and credit policy was definitely having a desirable effect on the economy, about as much effect as it should for the country's good in the long run. He expressed agreement with the degree of restraint that had been maintained up to the past three weeks. These three weeks had been difficult and he would be inclined to forget about them. In the period ahead, he would consider it desirable to liquidate enough of the System portfolio to maintain the restraint that existed prior to the past three weeks. He would not consider it wise to fix any amount of securities to be disposed of, and felt that this should be decided upon according to the feel of the market. He would not favor a change in the directive or the discount rate at the present time.

Mr. Fulton said that about the only thing he could report on the steel situation was that steel was being produced at a high rate. Fourth District mills were operating at approximately 97 per cent of capacity, which was above the national average of about 95 per cent. On or about January 7, a vote would be taken under the provisions of the Taft-Hartley Act to determine whether the latest proposal of the steel companies would be accepted by the workers; probably it would not be accepted. If not, and if nothing else were done, the strike would resume around the 27th of January. The companies were standing on an offer that would provide a package of 30 cents over a three-year period, this being about the extent of the improvement factor in steel production. The union was now following the technique of seeking agreements with the other industries served by it. Both the can and the copper industries had already signed up, and it appeared that the aluminum industry would enter into a contract containing a package similar to that agreed upon between Kaiser and the union in regard to that company's steel workers. The price of aluminum was lowered about two years ago because of overcapacity, lack of orders, and imports of aluminum. The industry felt that the current price was too low, and with a wage increase one could look forward to a possible price adjustment. There was no expectation of a sudden inflow of steel orders or any real pressure for deliveries in the first quarter of next year. Steel was coming in in quantities that were not expected, unusually large quantities in some cases. Warehousemen were getting adequate supplies, although not always in certain types of inventories. In the event of resumption of the steel strike, close-downs on the part of steel users were likely to be rather rapid and widespread.

Continuing his comments on the Fourth District, Mr. Fulton said that construction was 11 per cent under last year, while department store sales were 7 per cent above a year ago. Although there was considerable pressure on the banks for credit, the increase in loans had been gradual and bankers did not expect a surge of demand. Member banks had not been coming to the discount window to an inordinate extent.

Mr. Fulton commented that several Cleveland directors represented companies that had established plants abroad. At the last directors' meeting there was some discussion as to the present and potential effect of the establishment of such plants on employment in the United States. One director reported that the cost of tooling a new plant in Europe was only about 25 or 30 per cent of the cost in the United States. Another reported that workers at a plant in Japan were receiving for one day what American workers would receive in one hour. The general feeling was that considerable production was being lost to foreign plants established for the purpose of dealing in the countries concerned and also for the purpose of shipping certain products back to the United States. The directors expressed concern about profits of United States corporations from the standpoint of whether such companies would be able to compete with respect to ordinary run-of-the-mine products manufactured abroad.

Mr. Fulton did not feel that an increase in the discount rate at this time would be appropriate in view of the possibility of a resumption of the steel strike. He aligned himself with those who would retain a firm hand on bank reserves and, if possible, recapture the posture of restraint that existed prior to the relaxation which occurred incident to the release of vault cash. He would leave the directive in its present form under the premise that a change in the directive is indicative of a change in policy. In order not to get into a box by relaxing at this time if there should be a surge of activity after the first of the year, he felt that a firm hand was necessary.

Mr. Bopp said that developments in the Third District did not differ sufficiently from national developments to merit any particular comment. Steel operations were at 102 per cent of capacity, and district banks seemed to be under more pressure than banks throughout the country as a whole.

Despite the fact that, as the last three weeks had shown, data on reserves are not the only measure of restraint, Mr. Bopp felt that these data should be as good as possible. Therefore, the Philadelphia Bank planned to collect daily information on deposits and related items from member banks. The banks were to be asked to report on a prescribed form which would be sent to the Reserve Bank with the cash remittance letter. The Reserve Bank would process the data by machine tabulation, and at the end of each reserve computation period each member bank would receive a report showing its position. While the project was experimental, the Reserve Bank was optimistic that it would work out well.

Mr. Bopp said that he would favor continuing the present degree of restraint. He would be inclined to emphasize interest rate levels rather more than the level of reserves during this period. He would not recommend any change in the discount rate or the directive.

Mr. Bryan said that at the Atlanta directors' meeting last week the reports of branch directors and comments of the group seemed to indicate a great deal of optimism. He was puzzled as to whether to rely on such reports or on the statistics, for the latter tended to show a spotty situation, with no evidence of great boom in the Sixth District. Nonfarm employment was up only slightly, manufacturing employment and department store sales were down, bank debits were down significantly, demand deposits and currency had declined, and so on through the statistical series. Construction contracts were about

20 per cent under a year ago.

Mr. Bryan commented that district member banks were borrowing heavily from the Reserve Bank. Borrowings had been running rather regularly at over 15 per cent of the System total, whereas a figure of about 5 per cent would normally be indicated. While he did not know just what the cause of the borrowing was, some of it seemed to reflect the fact that loan totals in the district had gone up a little more rapidly than loans throughout the nation while the liquidation of investments had been more reluctant and considerably slower. The Reserve Bank was encountering a number of continuous borrowing situations.

As to policy, Mr. Bryan said he wished to associate himself with Mr. Mills who, if he understood correctly, approved a policy of restraint but had some fear that the System might overdo it and produce a deflationary situation. If there was no objection, Mr. Bryan wished to introduce into the record a chart and three tables which he felt had a bearing on a point he had made in the past, namely, that a situation appeared to be approaching in which the matter of the growth factor in reserves should have serious consideration. He felt that the System was now at that point, rather than approaching it, and he was willing to let the chart and tables speak for themselves. He also would like to introduce them because of his conviction, as stated from time to time, that one of the pertinent problems of the System and the Open Market Committee is to find a means by which instruction can be given in quantitative rather than qualitative terms. He said that he might wish to refer to the chart and tables at some later time for the purpose of furthering that discussion.

There being no objection, it was understood that the chart and tables referred to by Mr. Bryan would be made a part of the record of this meeting.1/

Mr. Johns expressed concurrence in the comment by Mr. Thomas that the greater danger was in too little rather than too much restraint. It appeared reasonable to expect that the demand for credit would rise greatly relative to savings in view of the expected behavior of inventories and other factors including consumer credit. It also seemed likely that the velocity of money would resume an upward course. Therefore, if inflationary deposit creation was to be avoided, he was of the opinion that bank credit expansion must be quite limited and that high interest rates--possibly increases--must be expected. In the circumstances, he would avoid any relaxation of restraint and even the appearance of relaxation. He was impressed by the fact that the discount rate was unusually low in comparison to the level of other short-term interest rates, that this situation had persisted, and that the spread had widened in the past week or 10 days. Therefore, he tended to favor an increase in the rate. However, if an increase was not to occur, he still felt confident

1/ Copies are attached to these minutes.

that restraint upon unwarranted credit expansion could be exercised through appropriate open market actions. He would not suggest any change in the directive at this time. With regard to the question of dealers' positions raised by Mr. Rouse, he concurred in the answer given by Mr. Mills.

Mr. Szymczak said that he had little to add to the discussion. He was impressed by the statements of Messrs. Mills and Bryan, if for no other reason than that he felt study was indicated regarding various means of measuring System judgments on policy. In his opinion, policy could hardly be changed at this time in view of the fact that the Treasury was about to go into the market and would stay in the market almost continuously for some time. In these circumstances, he would continue the policy that the System had been pursuing.

Mr. Balderston said that Mr. Bopp had encouraged him greatly by advancing the suggestion for measurement of money supply changes in the Third District. This, he felt, might be the most significant statement of the day. He would not want to change the directive until policy was changed, and he would not favor changing the discount rate until after the Treasury financing had been completed. By that time more might be known about the steel situation and also about the prospect of excessive movements in the economy. Between now and the next Committee meeting, he would favor retaining a firm position because he feared that errors on the side of ease might deceive many people, including the Committee. The time was not far off when the building of inventories could be resumed again as steel supplies became available, and he anticipated that loan pressures would be enhanced.

Chairman Martin said the impression he had of the money market at the moment, in the light of today's discussion, was that what the System did would not really make too much difference. During the discussion he had endeavored to keep a check of the views expressed, and on the basis of this tally it would seem difficult for the Account Manager to have any real indication as to whether the Committee favored more ease or more restraint. However, while one or two who had spoken seemed to favor a slight basic change in policy toward less restraint, he felt that the majority favored a steady policy.

The Chairman then stated that he would like to make one or two comments about the year as a whole which related to the present situation. First, it was his feeling that the System must be constantly on guard against taking itself too seriously. This comment applied to the measurement of net borrowed reserves and of degrees of restraint, or lack of restraint, more than in any other field. A man from Mars would think, perhaps, that by exercising a particular shade of restraint in the money market the Open Market Committee was going to make or break the economy in the course of a given period of time. While that comment, of course, was facetious, he felt that it did have a bearing.

Chairman Martin said that he was inclined to look upon 1959 as a satisfactory year for the System, although he felt sure that a great many people did not agree with System policy, because the System had maintained a consistent, intelligent, and understandable course. This probably was not true in 1958, and he was not sure that it was true in 1957, although he believed it was true in 1956. In 1959, however, the Federal Reserve had maintained a clear enough policy so that even those who disagreed were able to understand what the System was trying to do. He considered this encouraging, and he therefore thought of 1959 as a good year for the System.

When it came to the period immediately ahead, the Chairman said, he did not know whether it made a lot of difference how the System conducted itself as long as the System did not take itself too seriously. It seemed to him that the money market had a great many forces that no one could evaluate. Then, too, there was the balance-of-payments problem, now complicated by the boom in Europe. In a boom situation, attitudes with respect to cost-price problems are different than when a boom is not in process, and the pricing mechanism of the world tends to be out of joint. Attitudes on investment, including investment abroad, had changed markedly in the course of the last year, and there was today a shifting of capital all around the world.

Chairman Martin commented that all of these factors exerted an influence on prices and interest rates. This was a part of the ferment going on in the money market at the end of the year. Where he came out was that the System was going well, that it should keep steady in the boat, and that the problem was one of rolling with the punches at this juncture. This was not in any sense to say that the Committee should disregard Mr. Mills' basic point regarding the quantity of the money supply. Personally, he did not know just how to measure the money supply, but Mr. Mills was doing a service in bringing the matter up. Like many others, he (Chairman Martin) was unable to make heads or tails of the money supply on either a quantitative or a qualitative basis. For the year as a whole the increase in the money supply appeared to have been less than one per cent, and while he felt that this was more than offset by the increase in velocity, he could not prove it. In other words, while he believed that the increase in velocity adequately provided for growth he could not prove this statistically. This was where one got into the element of judgment. One should not go overboard on the money supply question unless he was certain that the velocity factor was not playing a part. Personally, he felt that money supply factors in terms of velocity were the crucial points that the System must take into consideration at this time. For this reason, he was wary about lessening restraint. With the optimism that was now in the picture, the question was not so much whether the System was going to have a tight rein on the money supply as one of gauging what the supply ought to be.

After commenting on prevailing public attitudes with respect to the use of credit, including credit at the consumer level, Chairman Martin said that this was a difficult problem for the System. He went on to say that he felt quite optimistic about the coming period. If one made a list of the problems with which the System was confronted, he could tend to get depressed. However, that kind of depression was not warranted; the problems, no matter how difficult, could be resolved. Indeed, it was the job of the System to deal with such problems.

In a further comment, Chairman Martin expressed regret that Mr. Riefler was going to retire at the end of this year.

Summarizing this meeting, the Chairman said that there appeared to be no question regarding the consensus. There should be no change in the directive, and a change in the discount rate was not favored at this time. He then inquired whether anyone disagreed with that statement of the consensus. When no comments were heard, the Chairman commented that this would stand as the consensus.

Turning to the question of the policy indicated by the consensus, the Chairman said he presumed that Mr. Mills wished to reiterate his previous position and have his comments placed in the record.

After Mr. Mills replied in the affirmative, the Chairman inquired whether there were others who would like to associate themselves with Mr. Mills and to have their views similarly recorded. Hearing no comment to such effect, the Chairman said that this would cover the vote on the policy indicated by the consensus.

With regard to the directive, Chairman Martin turned to Mr. Rouse and inquired whether he saw reason for a change, indicating that otherwise the directive would be retained in its present form. Mr. Rouse said he saw no reason for a change.

Thereupon, upon motion duly made and seconded, the Committee voted, with Mr. Mills voting "no," to direct the Federal Reserve Bank of New York until otherwise directed by the Committee:

(1) To make such purchases, sales, or exchanges (including replacement of maturing securities, and allowing maturities to run off without replacement) for the System Open Market Account in the open market or, in the case of maturing securities, by direct exchange with the Treasury, as may be necessary in the light of current and prospective economic conditions and the general credit situation of the country, with a view (a) to relating the supply of funds in the market to the needs of commerce and business, (b) to restraining inflationary credit expansion in order to foster sustainable economic growth and expanding employment opportunities, and (c) to the practical administration of the Account; provided that the aggregate amount of securities held in the System Account (including commitments for the purchase or sale of securities for the Account) at the close of this date, other than special short-term certificates of indebtedness purchased from time to time for the temporary accommodation of the Treasury, shall not be increased or decreased by more than $1 billion;

(2) To purchase direct from the Treasury for the account of the Federal Reserve Bank of New York (with

> discretion, in cases where it seems desirable, to issue participations to one or more Federal Reserve Banks) such amounts of special short-term certificates of indebtedness as may be necessary from time to time for the temporary accommodation of the Treasury; provided that the total amount of such certificates held at any one time by the Federal Reserve Banks shall not exceed in the aggregate $500 million.

Chairman Martin then referred to the suggestion that the next meeting of the Committee be held on January 12, 1960. He said he saw no objection, although the organizational meeting of the Committee should be held on March 1, 1960, which would fall on a Tuesday. This would mean having meetings at two-week intervals at some point. There would be some advantage in deferring the next meeting until January 12 because it might be possible to get additional information with respect to the year-end period. Accordingly, the meeting might be set for that date, at which time the Committee could decide what schedule it wished to follow thereafter.

In response to a comment by Mr. Hayes that an alternative would be to go four weeks between meetings on some occasion, the Chairman suggested that in the forthcoming period it seemed doubtful whether the Committee would want to let that long a period elapse.

After further comments, it was agreed that the next Committee meeting would be set for January 12, 1960, at which time the Committee would decide what to do about succeeding meetings. It was understood, however, the organizational meeting would be held on March 1, 1960.

Mr. Hayes commented that several persons at this meeting had referred to getting back to the posture that existed prior to the past three weeks, thus implying that the past three weeks had been quite easy. He took strong exception to that view, both from the standpoint of statistics and the money market atmosphere. As to the statistics, he noted that the level of net borrowed reserves had been higher, on average, during the past three weeks in spite of the release of vault cash; in fact, the figures might be interpreted to mean that there had been a tighter position during the last few weeks than earlier. This was confirmed by the general feeling of the banks and also the fact that short-term rates moved up quite sharply and averaged well above the preceding three weeks. On all counts, therefore, he dissented from the view that the situation was any easier during the past three weeks.

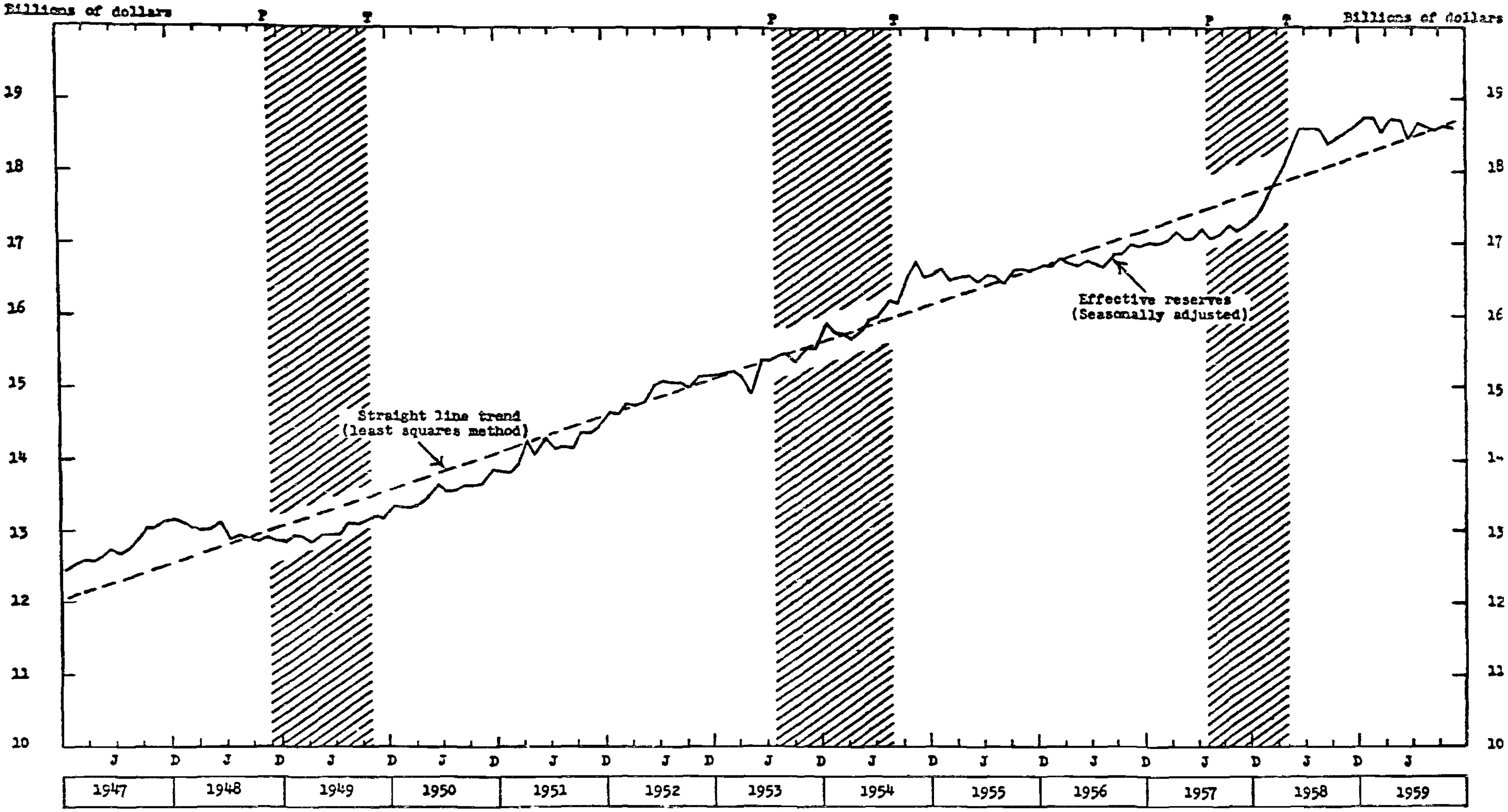
Mr. King said his comment had been intended to go to the point that the situation prior to the past three weeks presented a clearer picture and was less subject to controversy. Accordingly, he had suggested eliminating the past three weeks as a benchmark.

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

Following the executive session the Chairman advised that the Committee had elected Ralph A. Young as Secretary of the Federal Open Market Committee and Guy E. Noyes as Associate Economist, effective January 1, 1960.

The meeting then adjourned.

Assistant Secretary



Note: Shaded areas indicate recessions, according to reference dates of National Bureau of Economic Research. P = Peak; T = Trough.
Last month plotted: November 1959 Trend line exhibits an annual growth of 3.6 percent per year.

TABLE I

COMPOUNDED ANNUAL GROWTH RATES OF EFFECTIVE RESERVES*

(Percent changes, base year to terminal year)

Base Year	Terminal Year 1947	1948	1949	1950	1951	1952	1953	1954	1955	1956	1957	1958	1959 (11 mos.)
1947	x	1.8	1.0	2.0	2.6	3.2	3.1	3.4	3.3	3.1	2.9	3.3	3.0
1948	x	x	0.2	2.0	2.9	3.5	3.3	3.6	3.5	3.2	3.0	3.4	3.3
1949	x	x	x	3.9	4.3	4.6	4.1	4.3	4.1	3.7	3.4	3.8	3.6
1950	x	x	x	x	4.6	5.0	4.2	4.4	4.1	3.7	3.3	3.8	3.6
1951	x	x	x	x	x	5.4	4.0	4.3	4.0	3.5	3.1	3.7	3.5
1952	x	x	x	x	x	x	2.6	3.8	3.5	3.0	2.6	3.4	3.2
1953	x	x	x	x	x	x	x	5.0	4.0	3.1	2.6	3.6	3.3
1954	x	x	x	x	x	x	x	x	3.0	2.2	1.9	3.3	3.0
1955	x	x	x	x	x	x	x	x	x	1.3	1.3	3.3	3.0
1956	x	x	x	x	x	x	x	x	x	x	2.0	4.3	3.6
1957	x	x	x	x	x	x	x	x	x	x	x	6.6	4.7
1958	x	x	x	x	x	x	x	x	x	x	x	x	2.1
1959	x	x	x	x	x	x	x	x	x	x	x	x	x

*Reserve figures exhibited in Table I and the chart on effective reserves are total member bank reserves (monthly averages of daily figures) adjusted for changes in reserve requirements and for seasonal influences. No effort was made to remove the expansion potential of total reserves resulting from shifts in deposits among classes of banks and between types of deposits subject to different requirements.

Method of computation: For May 1958-November 1959, figures used are actual member bank reserves, adjusted for seasonal influences. Monthly values of effective reserves for January 1947 through April 1958 (when reserve requirements were last changed) have been derived by (1) obtaining the ratio of average required reserves to average deposits subject to legal reserves for May 1958-April 1959; (2) multiplying actual reserves by the percentage the above ratio is of the ratio of required reserves to deposits subject to legal reserves for each specified month; and (3) adjusting the values for seasonal influences.

TABLE II

COMPOUNDED ANNUAL GROWTH RATES OF THE U. S. ECONOMY

(Percent changes, base year to terminal year, of GNP in 1954 dollars)

Base Year	Terminal Year 1947	1948	1949	1950	1951	1952	1953	1954	1955	1956	1957	1958	1959 (3 qtrs.)
1947	x	3.9	1.8	4.1	4.9	4.6	4.6	3.7	4.2	4.0	3.8	3.2	3.5
1948	x	x	-0.2	4.1	5.2	4.8	4.7	3.6	4.3	4.0	3.7	3.1	3.4
1949	x	x	x	8.7	8.1	6.5	6.0	4.4	5.0	4.6	4.3	3.5	3.8
1950	x	x	x	x	7.5	5.4	5.1	3.4	4.3	3.9	3.6	2.9	3.3
1951	x	x	x	x	x	3.4	3.9	2.0	3.5	3.2	3.0	2.2	2.8
1952	x	x	x	x	x	x	4.4	1.3	3.6	3.2	2.9	2.0	2.7
1953	x	x	x	x	x	x	x	-1.7	3.1	2.8	2.6	1.6	2.4
1954	x	x	x	x	x	x	x	x	8.2	5.1	4.0	2.4	3.2
1955	x	x	x	x	x	x	x	x	x	2.1	2.0	0.5	2.0
1956	x	x	x	x	x	x	x	x	x	x	1.8	-0.2	2.0
1957	x	x	x	x	x	x	x	x	x	x	x	-2.3	2.1
1958	x	x	x	x	x	x	x	x	x	x	x	x	6.7
1959	x	x	x	x	x	x	x	x	x	x	x	x	x

TABLE III

COMPOUNDED ANNUAL GROWTH RATES OF PRICE INFLATION

(Percent changes, base year to terminal year, in Consumer Price Index)

Base Year	Terminal Year 1947	1948	1949	1950	1951	1952	1953	1954	1955	1956	1957	1958	1959 (10 mos.)
1947	x	7.6	3.2	2.5	3.8	3.5	3.1	2.7	2.3	2.2	2.3	2.4	2.2
1948	x	x	-1.0	0.0	2.6	2.5	2.2	2.2	1.6	1.5	1.8	1.9	1.7
1949	x	x	x	1.0	4.4	3.7	3.0	2.4	2.0	1.9	2.1	2.2	2.0
1950	x	x	x	x	8.0	5.1	3.6	2.8	2.2	2.1	2.3	2.3	2.1
1951	x	x	x	x	x	2.3	1.5	1.1	0.8	0.9	1.3	1.5	1.4
1952	x	x	x	x	x	x	0.8	0.6	0.3	0.6	1.2	1.4	1.3
1953	x	x	x	x	x	x	x	0.3	0.0	0.5	1.2	1.5	1.4
1954	x	x	x	x	x	x	x	x	-0.3	0.6	1.5	1.8	1.6
1955	x	x	x	x	x	x	x	x	x	1.5	2.5	2.6	2.1
1956	x	x	x	x	x	x	x	x	x	x	3.4	3.1	2.3
1957	x	x	x	x	x	x	x	x	x	x	x	2.7	1.7
1958	x	x	x	x	x	x	x	x	x	x	x	x	0.7
1959	x	x	x	x	x	x	x	x	x	x	x	x	x