

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, October 4, 1960, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Balderston
Mr. Bopp
Mr. Fulton
Mr. King
Mr. Leedy
Mr. Mills
Mr. Robertson
Mr. Shepardson
Mr. Szymczak
Mr. Irons, Alternate for Mr. Bryan
Mr. Treiber, Alternate for Mr. Hayes

Messrs. Leach, Allen, and Mangels, Alternate
Members of the Federal Open Market Committee

Messrs. Erickson and Deming, Presidents of the
Federal Reserve Banks of Boston and Minneapolis,
respectively

Mr. Young, Secretary
Mr. Sherman, Assistant Secretary
Mr. Kenyon, Assistant Secretary
Mr. Hackley, General Counsel
Mr. Thomas, Economist
Messrs. Brandt, Eastburn, Hostetler, Marget, Noyes
Roosa, and Tow, Associate Economists
Mr. Rouse, Manager, System Open Market Account

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

Mr. Patterson, First Vice President, Federal
Reserve Bank of Atlanta

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Messrs. Ellis, Ratchford, and Mitchell, Vice Presidents of the Federal Reserve Banks of Boston, Richmond, and Chicago, respectively
Messrs. Parsons and Coldwell, Directors of Research of the Federal Reserve Banks of Minneapolis and Dallas, respectively
Messrs. Arlt and Lynn, Assistant Vice Presidents of the Federal Reserve Banks of St. Louis and San Francisco, respectively
Mr. Stone, Manager, Securities Department, Federal Reserve Bank of New York

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the Federal Open Market Committee held on September 13, 1960, were approved.

Before this meeting there had been distributed to the members of the Committee a report of open market operations covering the period September 13 through September 28, 1960, and a supplementary report covering the period September 29 through October 3, 1960. Copies of both reports have been placed in the files of the Committee.

In supplementation of the written reports, Mr. Rouse commented as follows:

As the Committee has instructed, we have been operating primarily on the feel of the market rather than on the basis of reserve statistics, and this has involved the insertion of over \$400 million of reserves into the market since the last meeting. If the statistics have been helpful at all, it has been to point up the fact that for the time being, at least, higher levels of reserve availability have been needed to achieve the same degree of ease in the money market that existed earlier. A primary reason for this is the continued use of a heavy volume of credit by Government securities dealers, whose inventories continue at levels more than twice as large as we have come to regard as normal. In addition, there are indications that banks are

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putting the reserves supplied by the System to good use. Loans have been moving upward, and at the same time banks have been able to add somewhat to their investments. These results, which indicate that the money supply is continuing to grow, have taken place without any further downward pressure on interest rates.

Between now and the end of the year the Treasury will be involved in almost continuous financing operations. First, the schedule tentatively calls for a refunding of the one-year bills maturing October 17. This would presumably be through an auction, possibly with a paydown of \$500 million, so that the amount to be bid for would be limited to \$1.5 billion. The second operation would be a borrowing of about \$3 to \$3.5 billion of new cash around the third week in October, probably largely through the auction of a June tax anticipation bill, some of the proceeds of which could be used to make a paydown on the October 17 bills. In the first two weeks of November, there will have to be a refunding of the \$10.8 billion maturing bonds and certificates, of which the System Account owns \$5 billion. Whether this refunding will be done on a cash or exchange basis will depend on the state of the market at the time of the refunding. On top of all these activities, the Treasury is considering whether to have another advance refunding in the first part of December to extend some of the one-to-five-year debt into the five-to-ten-year area. A final possibility is that the Treasury may wish to refinance part of the Series F and G Savings Bonds maturing in early 1961 through an exchange offering before the year-end. There are about \$750 million of these obligations maturing next year.

The prospects for the Treasury's financing operations do not seem bright at the moment, since the market has not behaved well despite the underlying bullish influence of the economic situation. Speculative holders, as well as most potential buyers, are now following a "wait and see" course in view of the many current uncertainties. Heavy schedules of new corporate and municipal financing have also had a dampening influence, along with a sizeable overhang of those issues and the heavy inventories of Government securities in professional hands. Some announcement of Treasury plans is expected to be made later this week.

In reply to a question, Mr. Rouse said he would expect that the Treasury announcement would relate to the refunding of the one-year

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bills maturing October 17 and to the cash financing, with no mention of the refunding of bonds and certificates maturing in November, an advance refunding, or a refinancing of Series F and G Savings Bonds.

Thereupon, upon motion duly made and seconded, the open market transactions during the period September 13 through October 3, 1960, were approved, ratified, and confirmed.

A staff memorandum on recent economic and financial developments in the United States and abroad had been distributed under date of September 30, 1960. With further reference to economic developments, Mr. Noyes made the following statement:

At the mid-August meeting of the Committee, I suggested that one's conclusions from the information then becoming available depended heavily on the expectations which had gone before. This same observation seems to me to apply to most of the facts that have emerged in the last three weeks. The absence of a decisive movement in one direction or the other has left both the optimists and the pessimists without clear-cut confirmation of their expectations. Perhaps this has been illustrated best by the rather violent movements in the stock market in both directions.

On the plus side the increase in new orders for August attracted particular attention. The rise in orders received by fabricated metal producers and electrical machinery manufacturers was especially heartening.

The very rapid increase in loans and investments at weekly reporting member banks and the strength in the business loan component were also widely regarded as an encouraging sign--perhaps more so than all of the underlying facts would justify. I am sure Mr. Thomas will comment on these developments more fully, but for the purpose of this analysis of business developments it should be noted that the loan expansion has at least had some favorable psychological impact and has also demonstrated that the present posture of monetary policy is such as to permit banks to meet increased loan demands without further sales from their investment portfolios.

News which was released shortly after the last meeting that housing starts regained almost all of their July drop in

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August, and more recently that new construction put in place in September was also up slightly, provides some reassurance.

On the negative side, there is little doubt that the information on employment is the most discouraging news of recent weeks. After seasonal adjustment, both initial and continuing compensation claims showed a further rise in September to levels which have heralded or confirmed downturns in economic activity in the past.

The fact, not yet generally known, that the gross national product was probably down slightly from the second to the third quarter will almost certainly have unfavorable repercussions. Continued operations in the steel industry at only a little more than half of capacity, even as assemblies of 1961 autos expanded, and the failure to get even a seasonal rise in ingot output from August to September have been depressing influences. Both the number and liabilities of business failures, as reported by Dun and Bradstreet, have been running at or close to their postwar highs.

In the face of this mixed--but predominantly discouraging--information, attention has been focused more closely than ever on final takings, especially by consumers, for clues to the future course of business activity. From the weekly data for department stores and the ten-day reports on sales by automobile dealers, it appears that seasonally adjusted retail sales may be off a little from August to September. However, the last half of September appears to have been somewhat stronger than the first half.

There are continuing reports of price concessions, especially for durable goods, and some recent evidence that these may be generating a consumer response. It is noteworthy that in its August survey the Survey Research Center found a large number of consumers who stated they felt this was a good time to buy durable goods because of favorable price conditions.

In summary, there can be no question but that over-all economic activity has declined and is probably continuing to decline. It appears likely that the index of industrial production will drop another point in September, breaking out of the 109-111 range it has maintained so far this year.

On the other hand, most of the declines so far have been moderate. While it may be less than an even bet, it seems to me that there is still a possibility that the current downtrend may be reversed by the substantial easing of credit that has already been achieved, a favorable confluence of seasonal factors, including the seasonal shift in the Government's fiscal operations, and improved activity in some industries, such as steel, which have been producing below apparent consumption levels for several

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months. I might add, however, that I think this analysis suggests that the time within which such a reversal could occur is running out. If the downtrend is not arrested in the next few months--or at most before the first of the year--there would be much less chance that we shall avoid a deeper and more prolonged recession.

Mr. Thomas presented the following statement with respect to financial developments:

Bank credit developments in September were in some respects spectacular and apparently in contrast to other economic trends. Total loans and investments--at least of member banks in leading cities--increased more than in any other September of recent years. The increase began in the last week of August shortly following announcement of Federal Reserve action to supply additional reserves and to lower discount rates. At this stage, however, one cannot with certainty attribute these developments to an easier money policy, nor should a hasty conclusion be drawn that they are indicative of an upturn in economic activity, not yet shown by the economic indicators leading or coincident. Special factors can account for much, if not all, of the unusual increase in bank credit.

It can definitely be said, nevertheless, that System policies in the period made possible the increase without severe pressures on money markets and interest rates, even though they did not spark it. Furthermore, the availability of credit under the circumstances avoided unnecessary restraints that might have retarded economic activity. The longer-run significance from the standpoint of economic activity and Federal Reserve policy will depend upon further developments in the weeks ahead.

As to the facts, July and August were a period of moderate or slack credit expansion. Bank loans to business declined although some increase is usual for this period. New security issues by corporations and by State and local governments were larger than in 1959 but smaller than in many other years. Mortgage loan expansion was evidently also less than in other recent years. Growth in consumer credit slackened further and was less than a year ago. Federal Government borrowing was, of course, much reduced from last year, but banks increased their holdings of Government securities in contrast to a decline last year.

During September, in contrast, business loans at city banks increased by fully as much as in any previous September. Bank loans on securities increased much more than in the same month

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of previous years; and bank holdings of securities increased substantially whereas they usually decline in that month. New security issues were moderately large, although below previous high records. Total bank credit expansion, as previously stated, was larger than in any previous September. The increase was particularly large in the four weeks ending September 21. A greater than usual decrease occurred in the last week of September, but the record for the month still stands.

Special factors that may account for the exceptional bank credit expansion in September were (1) large Federal tax collections, along with heavy dividend and other payments customary in that month; (2) the absence of tax anticipation securities maturing in September; and (3) a shift in the liquidity position of corporations and perhaps of other businesses that has been developing this year.

Treasury receipts from all taxes were larger than in any previous September, reflecting principally heavy corporate income taxes payable in that month. In the previous two years, when corporations have been expected to pay one-fourth of estimated tax liabilities in September, not only were the amounts payable somewhat smaller, but also some of the payment could be made by turning in maturing securities.

Corporate liquidity, moreover, has been reduced since early this year. Cash balances have been drawn down some and the large holdings of Government securities built up in 1959 have been considerably reduced since February. Businesses, therefore, to meet large tax and other payments due in September, had to borrow from banks and also to reduce further their holdings of Government securities. The securities sold were purchased either by banks or by dealers, who in turn borrowed from banks. Expansion in business loans at banks, as already indicated, was little if any greater than the seasonal increase usual for September, and analysis of the details indicates that the increase was largely related to seasonal influences. Bank credit to cover tax and other payments was provided through the securities channel.

Most of the funds made available by this bank credit expansion have gone in the first instance to swell U. S. Government deposits, which increased by over \$2.4 billion in September to nearly \$7.5 billion at the end of the month. Generally, Treasury balances decline in September. Private demand deposits at banks increased sharply in the first half of the month, then declined by almost as much--at least at city banks. It is still uncertain whether they maintained the usual seasonal pattern, but preliminary estimates on a daily average basis indicate some further increase in the seasonally adjusted figures. In any event the sharp increase

in Government deposits did not cause private demand deposits to decline. Total money supply, seasonally adjusted, is probably about 1 per cent above the low level of last June, though still nearly 2 per cent below the peak reached in the summer of 1959. The rate of turnover of deposits in August was 7 per cent higher than a year ago.

In addition to the increase in Treasury deposits in September, time deposits increased further, continuing the marked upward trend evident since March. Such deposits at commercial banks have increased by over 5 per cent in the past seven months. For the year to date the accumulation of savings with the principal savings institutions has been somewhat less than a year ago. The decline, however, has not been as great as the decrease in direct investment of savings in credit and equity markets by businesses and individuals from the exceptionally high levels of last year. Since bank credit has expanded more this year than last, most of the decrease in the total flow of funds in credit and equity markets from the record \$62 billion in 1959 to around \$40 billion this year has occurred principally in direct investment by the nonfinancial sectors--consumers, businesses, and governments. These shifts no doubt reflect to some extent the effect of high rates of interest last year and lower rates this year.

One aspect of this change in the source of credit flows has been the weakness in the stock market during recent months. After reaching a new high level in July 1959, stock price averages generally fluctuated within a range of 10 per cent until mid-September of this year. In the past two weeks they declined sharply to the lowest average level since 1958, extending the range of fluctuation by about 5 per cent. This decline is related to a growing realization that corporate profits are not likely to be as large as had been anticipated.

Heavy demands for liquidity in recent weeks and the resulting pressures on banks and securities markets resulted in some rise of interest rates from the low levels reached in August. This rise has occurred notwithstanding actions by the System to make reserves readily available. Rates on three-month bills rose in mid-September to over 2-5/8 per cent for the first time since June. Though they have since declined to below 2-1/2 per cent, they are still well above the 2-1/8 per cent low reached early in August. Six-month bills have risen somewhat more in yield to around 2-7/8 per cent, compared with a previous low of 2-3/8 per cent. Treasury bill rates reflect in part the large positions that dealers built up in August, which made it difficult for them to absorb the pressure of selling by other holders to obtain cash that developed later.

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Rises in long-term rates have reflected in part the effect of the Treasury advance refunding operation and in part the volume of new offerings in the capital markets and dealers' enlarged inventories of such issues. Increases in yields on outstanding corporate bonds have been quite small, and those on U. S. Government securities also moderate, while yields on State and local government issues, where there has been somewhat more market congestion, have risen somewhat more.

Additional reserves to enable banks to meet the unexpectedly large credit and monetary demands in recent weeks have been liberally supplied by Federal Reserve operations. Reserves were made available in late August and early September through the release of vault cash and the reduction in requirements at central reserve city banks. These additions were partially offset by reductions in System holdings of securities, but on balance the total volume of reserves declined less than the seasonal decrease in reserve needs; not only did the money supply increase more than seasonally in August, but net free reserves also increased.

From the week of September 7 (which covered the reserve additions and ended just before the previous meeting of this Committee) to the week ending September 28, total member bank reserves increased by about \$320 million--somewhat more than had been projected three weeks ago. Required reserves increased by about \$100 million more than had been projected, reflecting principally a larger than expected increase in Treasury tax and loan accounts and at least the normal increase in other deposits. Gold movements and foreign operations absorbed about \$220 million of reserves--somewhat more than had been allowed for--but the difference was more than counterbalanced by reserves supplied in excess of anticipations through a return flow of currency and other factors. System operations actually absorbed reserves on balance in the three-week period, but heavy purchases toward the end of the latest week and in the course of this week, aggregating over \$500 million, will result in a substantial net addition to System holdings over the past four weeks. Free reserves have continued throughout the period close to or above the \$400 million level. Estimates for the current week ending tomorrow indicate a free reserve average of \$450 million or more.

Continuance of a relatively tight money market in the face of the increased reserve availability has been attributed in part to the distribution of reserves, with substantial excesses in country banks and shortages at city banks. Country

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bank excess reserves did increase sharply in late August and the first half of September, and since mid-September country banks have reduced their borrowings. Excess reserves have also declined since mid-September and in the past week free reserves of country banks have been little above average amounts held in July and August. It appears that the reserves made available have been largely put to use.

Probably a better explanation of the tightness at city banks is that the heavy demands for credit were largely concentrated upon those banks. They made use of all reserves available to them and also continued to be heavy purchasers of Federal funds from other banks. It is significant that city banks did not sell Government securities but added to their holdings, absorbing sales by other holders. Last week, operations in Federal funds were reduced; this was apparently because funds were less readily available for sale, as city banks temporarily increased their borrowings at the Reserve Banks. Whether this reduced supply of Federal funds indicates that other banks have been putting their excess reserves to use in loans or investments or is due to some other influence will not be clear until more complete data are available for the current period.

In the period immediately ahead, the most important credit market factor will probably be the drawing down of the large Treasury tax and loan accounts. In the next three weeks, assuming new Treasury financing payable October 24, the reduction in Treasury balances will exceed \$3 billion. The question is how these funds will be used as they pass to other hands. Will they go to increase private deposits? Will they be used to pay off bank loans? Or will they be employed for the purpose of buying Government securities from banks? Their impact on economic developments will depend upon various uses that will be made of the funds for spending or investment as they pass from one holder to another.

The normal seasonal increase in private demand deposits for the next three or four weeks is around \$2 billion and with a liberal allowance for growth should not be expected to exceed \$2.5 billion. Thus there can be some net contraction in bank credit and a decrease in total reserve needs during the three weeks until the next Treasury cash financing operation. In this period market factors are expected to supply reserves on balance, with substantial weekly variations and with a possibility that a larger than assumed gold outflow will reduce the net amount supplied.

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During the coming week, when currency demands increase and float declines, the supply of reserves will probably not be excessive and might even be augmented somewhat. In the subsequent two weeks some reserves might be absorbed by reduction in the System portfolio and still leave adequate amounts for any likely credit and monetary expansion. Retirement of outstanding repurchase contracts will absorb only a portion of the redundant reserves likely to be available at that time. System operations will need to be regulated according to the state of the money market.

After the week of October 26, the Treasury cash financing operation and then other seasonal influences will call for supplying additional reserves. If normal seasonal needs are met and free reserves maintained above \$300 million, additional reserves to be supplied by System actions will at times need to be as much as \$900 million, plus any sales made in the interim.

Mr. Marget made the following statement concerning the United States balance of payments:

When I last reported to this Committee, on September 13, I pointed out that on the basis of information then available, even if we were to receive no further orders with respect to gold purchases during the rest of September, net gold purchases by foreigners in September would be "about as large as in August." Actually, we did receive further gold orders, with the result that the gold figure for September, at \$315 million, was equal to the total purchases for the months of July and August combined.

We of course do not yet have the September figures for foreign-owned dollar balances. To the extent that we may take the figures for foreign dollar holdings at the Federal Reserve Bank of New York as a guide, the increase in foreign dollar balances in September may turn out to have been much smaller than it was in July and August. But there can be no doubt that the combined figure for the gold outflow and the increase in foreign-owned dollar balances during the third quarter of this year--this combined figure averaged about \$500 million a month in July and August, as compared with a monthly average of \$280 million in May and June--will be such as to invite widespread comments on what will undoubtedly be generally characterized as a deterioration in our balance-of-payments position. One can only hope that the more influential of these comments will be well informed.

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It would not be well-informed, for example, to fail to observe that the "deterioration" in question can in no sense be interpreted as indicating a worsening in the trade account of the kind that, in 1958 and up to the middle of 1959, was the source of such widespread concern with respect to our balance of payments. In my last report to this Committee, in commenting on the July trade figures, I pointed out that our trade surplus had risen from around zero a little over a year ago to a figure of around \$5 billion. This conclusion is not significantly changed by the latest figure, which we now have, giving a preliminary total of exports for August. This August figure, while it is below the July figure (the height of which reflected mainly a bunching, in that month, of jet aircraft shipments and large end-of-season exports of raw cotton), was still slightly above the relatively high average May-June rate. With imports remaining relatively steady, it is therefore quite clear that the cause of the "deterioration" in our over-all balance of payments that began in July has not been due to a deterioration of our trade position.

It is equally clear, on the basis of other information at our disposal, that a major cause of the "deterioration" has been an increase in short-term capital outflow, which in turn has been significantly affected by the differences in the level of interest rates here and abroad. It is to be hoped that public comment on the "deterioration" of our balance of payments in the third quarter of this year will take adequate account of this fact, and will not misread its implications. It is a fact, for example, that some countries, in presenting their balance-of-payments results, would not regard this kind of capital outflow as affecting the balance of payments at all, on the ground that the increase in short-term claims on us which is created by the capital outflow is matched by our equivalent item of short-term "claims on foreigners." (This was borne in on me strikingly this last week when the distinguished governor of one of the European central banks--who happens also to be an economist--asked me whether we did in fact treat short-term capital outflow as a factor affecting the over-all deficit in our balance of payments. I should add that he then added immediately that it was probably natural that we should do so, since, as a country with a "key currency"--that is, a currency which is very widely used as a reserve currency by other countries--we did not regard anything but gold as part of our reserves, even though in practice we might expect that the

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reserves "lost" as a result of an unfavorable international structure of interest rates could be expected to flow back when this structure of interest rates changes.)

There is in fact no evidence, as yet, of any action by foreign monetary authorities with respect to their dollar balances which would indicate that they do not understand this fully. But this is not the same thing as saying that these authorities are necessarily fully convinced that we are close to a solution of our balance-of-payments problem as a whole. On the contrary, we may expect that renewed public discussion of the size of our balance-of-payments deficit, in conjunction with discussion of the continuing gold outflow, will lead to a renewed posing of this basic problem, which has far more serious implications than the particular matter that is now so much in the center of public discussion; namely, the intensification of gold outflow in relation to short-term capital movements induced by interest-rate differentials.

It is possible, indeed, that this renewed public discussion of the basic problem may start with the citation of a passage, which has already attracted considerable attention, in a speech made a week ago yesterday by Per Jacobsson, the Managing Director of the International Monetary Fund, at the Annual Meeting of that organization here in Washington. "There is now," he said, in speaking of the U. S. balance of payments, "a substantial trade surplus, which for the whole of 1960 may exceed \$4 billion and which, with net income from investments and other invisible receipts, may well amount to \$6 billion." "This," he said, "would be sufficient to cover fully the present rate of U. S. Government expenditure abroad, including military expenditure and economic grants and loans." This, to be sure, would leave uncovered not only "the outflow of short-term funds" but also "the export of long-term capital on private account." "Nevertheless," he said, "these movements--and the same is true of government loans--have as their counterpart the acquisition of foreign assets, and in this way are somewhat different from an outflow of funds resulting from a deficit on current account."

This is, of course, true; and it should provide something of a corrective for any likening of the balance-of-payments position of the United States to that of countries which, unable to balance their current accounts and acquiring no claims on foreigners as a counterpart for their reserve losses,

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are in effect living on their capital. But there, one fears, the crumb of comfort ends. For the United States is in the position not only of a great trading nation and a great lending nation: it is also in the position of a banker. That is to say, it has to be concerned also with its liquidity position; and from this standpoint it is small comfort to be told that long-term claims are being built up against foreigners if a considerable part of these long-term claims are being matched, not by exports which would definitively discharge our obligation to deliver real resources to those to whom we lend, but by short-term claims against us held by those countries which did deliver the real resources. In contrast to the position created by the movement of short-term capital in which short-term claims on us are matched by our short-term claims on foreigners, we would be in a position of borrowing short and lending long, a process which, to put it mildly, has been shown to have limits, in international as well as in domestic finance.

What this amounts to saying is, of course, that as long as the nontrade international commitments of the United States remain at their present level (to say nothing of their going even higher as the result of new commitments for foreign aid), our export performance, good as it is by comparison with the grinding decline in exports from 1958 to the middle of 1959, is still not good enough; and that it will not be good enough until our over-all accounts are effectively in balance, so that it will not be necessary, in order to settle our accounts with foreign countries, to transfer gold and dollars to them. One must add to this, and indeed one must underscore heavily, the further caveat which Mr. Jacobsson himself added: "It must be borne in mind that the improvement which has occurred in the U. S. current account this year, while it is basically an important development, results from some special factors, particularly the strong boom in other industrial countries. It is, therefore, too early to conclude that the United States' payments difficulties have been fully overcome, and continued vigilance is required."

This is a reasonable, balanced statement to which one can subscribe. It does not say, and does not imply, that our balance-of-payments problem is so serious, as of this moment, as to deprive us of all flexibility in our efforts to cope with the requirements of the domestic situation. It simply states a proposition which ought to be regarded as virtually self-evident; namely, that the requirement of flexibility cannot, in the current situation, be interpreted as permitting

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a range of action as unlimited as it might have been if our basic balance-of-payments position were different from what it is in fact.

Mr. Treiber presented the following statement of his views on the business outlook and credit policy:

Recent economic activity has been disappointing. The seasonal upswing customary at this time of the year lacks its usual vigor. On the other hand, there is no evidence of serious deterioration.

With retail sales showing no increase and manufacturers' sales declining, business concerns are very cautious on their inventories. Surveys of business plant and equipment expenditures point to a leveling off or decline in capital spending. On the other hand, some August developments hint at the possibility of an upswing in the home building sector. In addition, Federal Government defense spending is being stepped up slowly, and State and local governments are expanding their construction outlays. The hesitancy in consumer demand, the leveling tendencies in business demand, and increased domestic and foreign competition have been reflected in an unannounced easing of prices of many types of manufactures. There is little evidence as yet, however, of aggressive price reductions aimed at increasing volume.

Economic activity in Europe is strong, although there are some signs that the expansion is moderating. Because of our balance-of-payments deficit, foreign official holdings of dollar assets continue to rise. And there has been a further outflow of gold reflecting the practices of foreign central banks with respect to the portion of their reserves to be held in gold. The recent stream of foreign visitors has emphasized the concern abroad lest the United States fail to take adequate measures to correct its balance-of-payments deficit, and lest it succumb to excessive monetary ease and fiscal laxity.

Our most recent studies of the Treasury's prospective income and expenditures indicate some reduction in the estimated cash surplus for the current fiscal year. Such a change would, of course, reduce the contractive effects of a budgetary surplus.

There continues to be a good demand for bank credit. Although the demand for business loans since mid-year has been less vigorous than it was last year, the demand was strong in

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September. The poorer record in August reflected in part a shift from bank borrowing to financing through commercial paper to take advantage of a rate differential. The volume of commercial paper, finance paper, and bankers acceptances has increased substantially. The rise in member bank reserves in September suggests that a base has been provided for a further increase in the money supply.

Short-term interest rates, as measured by the three-month United States Treasury bill, are nearly half of what they were at the beginning of the year. Other short-term rates have declined substantially, but not as greatly as the bill rate. Mortgage money is more readily available, but rates are sticky. I wonder to what extent a further decline in mortgage rates might stimulate construction, for I think we would not want to see additional construction held back because of inadequate credit.

Although the Federal Reserve has contributed greatly to credit availability, the decline in long-term interest rates has been quite modest. This may be one of those times, arising once in a while, when it may be well for the Committee to consider the extent to which a further reduction in long-term rates might contribute to economic activity.

Interest rates abroad, particularly for money market assets, are much higher than interest rates in the United States. Therefore, there is some attraction to investors, both foreign and American, to move funds abroad. We must bear this in mind in considering the level of interest rates in the United States, particularly the level of short-term rates.

It is important that the United States act promptly and wisely to rectify its balance-of-payments deficit. Failure to do so will more and more circumscribe the ability of the Federal Reserve to pursue a flexible monetary policy. Indeed, it may no longer be practicable for the Federal Reserve to seek to bring about a substantial reduction in long-term rates by helping to produce a very low Treasury bill rate and other short-term rates.

In our opinion, business and credit developments counsel a continuation of the policy of credit ease. We should avoid, however, driving short-term rates much lower; to do so would intensify our balance-of-payments problems without promoting any real advantage domestically. We see no reason for a change in the directive or a change in the discount rate. Later this

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week the Treasury will announce its plans for refunding the one year Treasury bills maturing October 17, 1960, and for raising additional cash. This prospective Treasury financing counsels the maintenance of an even keel in the money market.

While reserve requirements and margin requirements are not within the jurisdiction of the Committee, it seems to us that some time this fall it may be opportune to reduce further the reserve requirements applicable to central reserve city banks, bringing closer to fulfillment the Congressional mandate to abolish the differential between central reserve cities and reserve cities. As for margin requirements, we tend to think of a margin requirement of 50 per cent as a normal requirement. Recent events in the stock market would seem to indicate little need for continuing the present degree of restraint on the availability of credit for the purpose of purchasing and carrying securities.

As for open market operations, we believe that the Committee should seek to maintain a comfortable money market atmosphere. This would mean, for example, that the Federal funds rate should frequently be below the discount rate. On the other hand, it would seem important to avoid any substantial decline in the rate on three-month Treasury bills. We think that the Manager should be given wide latitude to supply reserves according to the tone of the market.

Mr. Erickson reported that the sideways movement in the First District had continued, with no apparent strong tendencies either upward or downward. As he had reported earlier, the New England production index went up from 118 in May to 124 in June; in July it dropped to 122, the same as in July 1959. What the index would do in the future remained to be seen, particularly with 30 to 40 thousand people out of work in the area because of a continuing strike. The Dodge figures on construction contracts in August showed a gain of 19 per cent, the best since April 1959. The increase was 64 per cent in nonresidential contracts and 5 per cent in residential, with increases in all categories except utility

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companies. The cumulative figure for the first eight months of the current year lagged 9 per cent behind the previous year, however, primarily due to a 40 per cent drop in public works and utilities. The gain in non-agricultural employment from July to August was the same as last year, but the unemployment situation had worsened, as it had nationally; the volume of new and continued unemployment compensation claims was substantially higher than last year. For the first eight months of the year, the cumulative figure on department store sales was 3 per cent above the previous year. In July, new car registrations were up, whereas they were down nationally; for the first seven months of this year, registrations were 18 per cent above 1959, this increase also being greater than the national figure. The survey of mutual savings banks for September had not yet been completed, but in August sales of Series F and G Savings Bonds increased over July and redemptions decreased. The rate of redemptions over sales was the lowest since February.

Business failures in the District were less than in the previous year, though in August they were greater than in the same month of 1959. New incorporations had been more favorable in New England than nationally in each month since March.

In the past three weeks District banks were substantial buyers of Federal funds, Mr. Erickson said. Borrowings at the discount window amounted to \$10 million or more on only four days, and averaged around

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\$6 million. The heavy borrowings were on days when the larger banks could not buy Federal funds.

Mr. Erickson stated that he would favor no change in the policy directive or the discount rate. In his opinion the Desk had done an admirable job in supplying reserves aggressively, and he would favor issuing the same instructions as before. He would supply reserves as needed, and if the Desk should anticipate the need for reserves somewhat he would not object. He had been pleased to see the Federal funds rate below 3 per cent on a number of days, and he hoped that this would continue to be the case in the next three weeks.

Mr. Irons reported that, broadly speaking, conditions in the Eleventh District were similar to those prevailing nationally. Activity was moving along in sideways fashion on a high plateau, with mixed forces underlying the total. On balance, however, there may have been some slight weakening during the past three weeks, and some indicators were a little less favorable. The index of production was down, and until recently department store sales were off somewhat. On the other hand, construction had improved substantially, as reflected by contract awards, and the agricultural situation, although marked by some spottiness, was good in total. In Texas, unemployment had declined a bit.

Mr. Irons said that demand and time deposits of District banks were up during the past three weeks, as were loans, and that reserve

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positions were somewhat easier than several weeks ago. On balance, District banks had been sellers of Federal funds; only one large bank had been a persistent and substantial buyer of Federal funds. Borrowings at the Reserve Bank were comparatively light, averaging around \$12 to \$14 million, with practically all of the activity accounted for by smaller banks borrowing for seasonal reasons. The one large bank mentioned previously had come to the discount window on a few days when Federal funds were not available.

Mr. Irons noted that there were some factors that might be considered neutral. Employment was just about the same as a year ago, and there had been no change recently in the petroleum situation. Psychologically, there did not appear to be an attitude of pessimism, but more an attitude of reconciliation to the point of view that there was not likely to be too much change one way or the other.

Mr. Irons expressed the view that during the past three weeks the operations of the Desk in carrying out Committee policy had been most satisfactory. Developments had been favorable from the System's standpoint. There had been a substantial expansion in bank credit and the increase in the money supply so much desired was being achieved, while at the same time it had been possible to avoid pressing down short-term rates substantially. He would like to see approximately the same policy continued, without any attempt to force further ease aggressively.

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He would meet seasonal requirements and, as best as could be determined by the feel of the market and other factors, the requirements for essential and reasonable loan expansion. However, he would avoid a degree of ease that would tend to push short-term rates substantially lower. In his opinion a market position reflected by a bill rate fluctuating from 2-1/4 to 2-1/2 per cent, a Federal funds rate from 2-1/2 to 3 per cent, and member bank borrowings in the area of \$250 to \$400 million would be appropriate in the present situation. He would not recommend any change in the directive or the discount rate at this time.

Mr. Mangels said that the Twelfth District picture was somewhat mixed. In the West Coast States there had been a further decline in employment, and unemployment was at a rate close to 6.5 per cent. On the other hand, there was an increase in both residential and non-residential building awards in August, which was somewhat unusual because that month normally shows a decline. While both categories were up 19 per cent from July and nonresidential contract awards were about 18 per cent higher than a year ago, the residential figures were still somewhat below 1959. Steel production had improved somewhat in the past few weeks, with operations increasing from 52 per cent to 55 per cent of capacity, this having been due in part to a rather large order for pipe for a natural gas transmission line to Canada. There had also been some improvement in the demand for reinforcing bars and tin plate, and people in the industry seemed to feel that the steel

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problem might be bottoming out. There appeared to be somewhat the same feeling in the lumber industry, although output was still down, inventories were remaining constant, and orders had not increased. Fir prices had softened, but plywood prices had increased because of the rather substantial curtailment of production.

Department store sales were about 3 per cent below a year ago in the four-week period ended September 21, and it appeared that sales for the month of September might show a 3 to 4 per cent decline from August. New car registrations in California were lower in August than in any other month this year, but information for September indicated a substantial pickup in sales as compared to 1959. The farm situation apparently was not as good as had appeared at mid-year, with some reductions in market prices and in estimates of crop output. Some farmers in California were still having difficulties with the unions; it was reported that in some cases crops were being plowed under. The cattle situation seemed to be a little better; there were 24 per cent more cattle on feed lots in California than a year ago.

Mr. Mangels reported that loans of District banks increased slightly in the four-week period ended September 21, mostly in the week ended September 14 due to borrowings for tax purposes. Real estate loans declined and although consumer loans increased, outstandings were somewhat below mid-year. Demand deposits increased slightly and time deposits also were up. It was rather encouraging to find savings deposits

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increasing, even though at a somewhat lower rate than at savings and loan associations. District banks increased their holdings of Government securities about \$140 million in the past three weeks; they were net purchasers of Federal funds to the extent of about half a billion dollars in the past week and estimates for the current week were about the same. Borrowing from the Reserve Bank had been nominal; one substantial borrowing last week was reportedly due to inability to obtain Federal funds. In some areas, banks reported that they were in a rather tight position.

Mr. Mangels said it was his feeling that a policy of ease should continue. The projection for free reserves of \$480 million for the week ending tomorrow was about what he had in mind; that is, free reserves around the \$500 million level. The prospect of a further decline in general business activity seemed to him to be greater than any possibility of an increase. If action were taken in the early stages, it would do more good than if the System waited until later, and if the situation should improve it would be quite easy to reverse quickly. The period was approaching when the usual seasonal demand for loans could be expected, and reserves should be supplied freely. Also, the time was approaching when the Treasury would be in the market frequently and an even keel policy would be required. As quickly as possible, therefore, he would supply additional reserves on a rather liberal basis. As he had indicated,

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he would try to maintain free reserves of around \$500 million or a little higher. The discount rate and the directive seemed to him to be quite proper.

Mr. Deming reported that Ninth District economic developments were mixed, and that opinions also were mixed regarding the outlook. Viewing the picture broadly, agricultural conditions showed considerable improvement over a year earlier, trade and industry revealed some tendency to slacken, although this was not consistent from area to area, and bank liquidity positions had been eased.

The District farm outlook seemed excellent, Mr. Deming said. Cash receipts in the 1960 crop year (from mid-1960 to mid-1961) should be about 5 per cent greater than in the preceding crop year, due largely to improved crop output, and it appeared that net farm income might increase as much as 20 per cent. If so, this would mean an increase of perhaps 2 per cent in total personal income in the District from this factor alone. The four weeks ended September 21 showed the largest gain in bank deposits for any comparable period since 1950 while loans and investments increased at a lesser rate, resulting in a reasonably good improvement in member bank liquidity positions. Purchases of Federal funds and borrowings at the Reserve Bank both had declined quite substantially. While industrial activity in the District appeared to have slackened in recent months, at least on a seasonally adjusted basis, both in durable and nondurable manufacturing, mining activity compared

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favorably with a year ago, reflecting primarily the effects of strikes last year in both copper and iron ore. Construction activity seemed to be moving upward, but retail sales during September were disappointing.

Mr. Deming said he saw no reason to change either the directive or the discount rate. As to open market operations, he wished to associate himself closely with the position of Mr. Irons. The Desk had done a good job in the past three weeks, and he would like to see the Desk allowed to continue to operate with wide latitude. He would meet seasonal requirements as they built up, but not press too aggressively for additional ease in the market. His summarizing comment was that "we are about where I would like to see us stay for at least the next three-week period."

Mr. Allen noted that the Federal Reserve staff summary referred to diverse views on the business situation and said that such views were expressed at the meeting of the Chicago Board of Directors last week. Some saw signs of improvement while others, incidentally a majority, could find no basis for optimism. However, it might be representative of an unrecognized confidence that not one of the directors wanted to reduce the discount rate, whereas two weeks earlier a few of them had felt that another reduction might be in order.

Mr. Allen said that department store sales in the Seventh District, while making a poor showing during the first part of September, were three per cent above last year in the week ended September 24. Steel

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operating rates continued higher in the District than in the country as a whole. The mills in Chicago were doing better than 60 per cent of capacity and the rate in Detroit was about 70 per cent. Some of the machine tool industry's executives reported that the improvement in orders in August continued in September. Another promising note was that new business generated at the Machine Tool Exposition was not expected to show up until October and November.

On the other hand, unemployment claims continued heavy. In the first three weeks of September such claims were 60 per cent over last year in the Seventh District, compared with 37 per cent for the country. Unemployment appeared to be heavily concentrated in the industrial areas; the Reserve Bank's Personnel Department and those of the commercial banks in Chicago had found no appreciable easing in the job market.

Farm and construction machinery firms had been reducing production. Recently, International Harvester announced a temporary lay-off of 17,000 workers in a number of plants throughout the country, the purpose being to reduce inventories. However, Harvester reported that sales to farmers had improved recently, and the same report came from Allis-Chalmers.

Automobile production was being increased gradually, but not so rapidly as originally scheduled, Mr. Allen said. Although sales for September continued to be estimated at about 400,000 cars, which

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would be an improvement of 14 per cent over September 1959, the major source of concern continued to be the load of 1960 model cars still in dealers' hands, with the concentration in medium-priced lines. If production and sales estimates for September were realized, stocks on September 30 should have been about 900,000 units, including 440,000 1960 models and 460,000 1961 models. That number of unsold old models would be 100,000 higher than on the same date last year and would, it was generally believed, restrict 1961 model sales for several weeks.

Mr. Allen went on to say that for what it might be worth as an indicator, the amount of space in Chicago newspapers utilized to advertise for help in September was 17 per cent below September of last year, and had shown a steady decline since March. The amount of advertising lineage was one-third below the relatively high level in the first quarter of 1960, but it was 50 per cent above the level reached during the first half of 1958.

Information received from large Seventh District banks in the quarterly interest rate survey indicated that the prime rate cut was followed by a significant decline in the rates actually charged on business loans during the first half of September. The average rate for all loans made during this period dropped to 4.93 per cent, from 5.33 per cent last June. As would be expected, the cut showed most for the largest loans, but was reflected to some degree in all size categories. Moreover, a larger proportion of

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the total number of loans reported in September was made at the prime rate than in the previous survey.

For the most part, Seventh District banks continued to enjoy lessened reserve pressures. The basic position of the Chicago central reserve city banks had fluctuated between small surpluses and small deficits. In dollar amount, the bulk of borrowing at the discount window during the last month had been concentrated at a few large banks in Detroit and, to a lesser extent, Milwaukee. Borrowing by country banks had continued to decline in amount, frequency, and number of borrowers.

Mr. Allen said it was his feeling that in the area of monetary policy the Committee should carry along as in the past three weeks. He would not change the discount rate or the directive, and he would seek to maintain the current degree of ease in the money and credit picture. He supposed that the pending Treasury financing argued for a policy such as he had suggested for the next three weeks, but he would favor it even if a new Treasury issue were not on the table.

Mr. Leedy said there had been no new developments in the Tenth District of enough significance to warrant summarization. As had been mentioned several times, policy for the forthcoming period would seem to be dictated largely by the Treasury financing program, which would call for maintaining an even keel. Aside from that, however, it seemed to him that economic considerations, both nationally and

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as far as the situation in the Tenth District was concerned, would indicate a continuation of the policy that had been followed during the past three weeks. He wished to associate himself with those who felt that the Desk had done a good job during this period. Some of the objectives of the Committee had been achieved, including increases in the money supply and in loans and investments. For the period immediately ahead, he saw no necessity for changing what had been done during the past period.

Mr. Leach reported that business activity in the Fifth District continued to show only small changes, with perhaps a majority of them pointing downward. A gradual but steady decline in District man-hours in manufacturing, seasonally adjusted, had been in progress since May. Employment in trade remained steady, while in financial institutions, service industries, and government it had increased. Production in the textile industry, which was curtailed three or four weeks ago, had apparently stabilized at the reduced level. Textile prices remained soft but had not declined significantly, and leaders of the industry continued to regard prospects as mildly favorable. Furniture makers in the District reported normal seasonal strength, both in new and unfilled orders, and expected to complete the year without much change. Construction employment in the District remained at or near its highest level, set in May of this year. Construction awards already made and the volume of

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construction currently in process were significantly higher than a year ago and probably assured the industry of a high level of activity for the remainder of the year. Farm income prospects remained good in spite of crop damage by hurricane Donna, which was severe in certain localities. Retail trade was fairly steady at a level slightly below that of a year ago.

Mr. Leach commented that Fifth District banks were definitely in an easier position than at the time of the previous Committee meeting. Total loans of weekly reporting member banks rose more than during comparable weeks of any recent year, but the percentage increase in investments was twice as large. Deposits increased sharply and loan-to-deposit ratios dropped from 54 per cent to 52 per cent. Average daily borrowings at the discount window had been quite low, and money market banks had been heavy net sellers of Federal funds.

With respect to policy, Mr. Leach said he thought the Committee had eased enough for the time being and should stand pat for the next three weeks. The reserve position of member banks was now quite a bit easier than it had been earlier, and he saw nothing to be gained by driving short-term interest rates down from existing levels. More ease, in his opinion, would not be of material assistance to the economy, but would affect the balance of payments adversely and could make the task of monetary policy more difficult in the future. In determining the prevailing degree of ease, he thought the Account

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Manager might give somewhat more than the usual attention to short-term rates. It seemed to him that the System was in a very good position to follow the even-keel policy that was called for by the Treasury financing. He saw no reason to change the directive or the discount rate.

Mr. Mills commented that in the normal course of policy making the actions of the Open Market Committee had been governed by a cautious interpretation of, and alignment of policy actions with, statistical evidence of movements in the economy. However, since the best of statistics relate to past events and since the economy was unquestionably experiencing a rapid period of change, in his opinion there was a good case for taking a much more imaginative approach to policy actions that would speculate further into the future and move out of the realm of dead statistics. To implement a policy of that kind which would require a resourceful adaptation to evidence that might be foreseeable but was not yet clearly visible on the horizon, he wished to offer a statement which in effect did not contemplate any major change in the supply of reserves that was put at the disposal of the commercial banking system but involved the choice of a different vehicle for supplying those reserves.

Mr. Mills then presented the following statement:

In the light of past experience, a minimum volume of member bank borrowing at the Federal Reserve Banks and a low level of positive free reserves would have supported a marked expansion of commercial bank credit and brought about a sharp reduction in interest rates. That not having been the case leads to the conclusion that the drag of recessionary financial forces has tended to overcome the intended effects of an expansionary Federal Reserve System credit policy.

The most striking indications that this kind of situation exists are a tight money market in the midst of easy commercial

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bank reserve positions, sluggish and falling markets for U. S. Government securities and other types of fixed interest obligations, and an abrupt increase in commercial bank time deposits.

As regards the tight money market, the evidence suggests that slackening business activity has set up contractive financial forces that are drawing funds into the major financial centers which are then employed by important borrowers to apply on their bank indebtedness, with the consequence that demand deposits, both from the outlying banks from which they have been withdrawn and from the main depository banks of such borrowers, are subjected to downward pressure. These financial movements may account for the tight condition of the money market.

As regards the ragged market performance for U. S. Government securities, the evidence suggests that slackening business activity has reduced the turnover of inventory and accounts receivable investments of commercial and industrial concerns to the point of compelling a divestment of some proportion of their holdings of short-term U. S. Government securities in order to avoid having to compress their sales and inventory activities. The divestment of U. S. Government securities that has reflected these pressures on corporate liquidity positions has resulted in an outflow of such securities from corporate hands that, as it has been absorbed only partially into the commercial banking system, has lodged in the unusually heavy positions of the U. S. Government securities dealers. It would, therefore, appear that a direct relationship exists between the contractive financial forces that seem to account for tight money market conditions and the poor performance of the U. S. Government securities market in the face of a nonrestrictive Federal Reserve System credit policy.

As regards the increase in commercial bank commercial and individual time deposits, the available evidence suggests that this phenomenon is also attributable to slackening business activity, with a consequent unwillingness of the holders of such deposits to employ them more venturesomely.

The determination of a Federal Reserve System monetary and credit policy that will constructively counteract the financially depressing economic factors that have been discussed is difficult. The fact that U. S. Government securities are coming onto the market in greater volume than the market's absorptive capacity, and that time deposits have been the chief vehicle used by the commercial banks to acquire U. S. Government securities, gives reassuring evidence that what might otherwise have been a superfluity of reserves placed at the disposal of the commercial banking system will not erupt at any foreseeable date into a

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major expansion of bank credit that would force interest rates down to undesirably low levels. As a matter of fact, the real problem seems to be how to develop a Federal Reserve System monetary and credit policy that will counteract the contractive influences that are bearing down on commercial bank deposits. Inasmuch as these contractive forces will increasingly have their initial effects on the deposits of the country banks and the smaller reserve city banks, it would be logical to adopt policies that will sustain the deposit positions of these banks and prevent a spiraling contraction of deposits at all classes of banks. In the light of recent experience, open market policy actions supplying reserves have not induced a credit expansion at the outlying banks sufficient to offset the down pull on their deposits. More positive action seems necessary, and conceivably should take the form of a reduction in the reserve requirements for the country banks. Coming directly into the possession of additional reserves through this policy action the country banks might be expected to employ them in the acquisition of short-term U. S. Government securities, thus creating new deposits as a buffer against potential deposit losses arising from previously described circumstances at the same time that a modest strengthening of influence would have been thrown behind the U. S. Government securities market.

Mr. Robertson said it seemed to him that the policy of providing additional reserves that the Committee was following had been working well. The reserves had been put to use, not only in the expansion of bank loans but also to improve the liquidity positions of the banks of the country, which augured well for the further loan expansion that would be needed. Consequently, there was good reason to believe that the Committee had been on the right track, and it should stay on that track.

Mr. Robertson said he was impressed by a comment Mr. Noyes had made to the effect that a great deal was going to depend on what happened in the next two or three months. Therefore, if the policy that had been

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followed was good up to this time, it would appear, in the absence of Treasury problems, that the Committee ought to enhance the degree to which reserves were made available. However, it seemed to him the Treasury position was one that bound the Committee and that it was necessary to maintain an even keel. Nevertheless, he would do everything possible to provide additional reserves within the concept of even keel. He would not permit tightness to develop in the market any more than it had been permitted to develop during the past three weeks.

Mr. Robertson said that he would not recommend changing the policy directive, and that the discount rate could hardly be changed at this stage of the Treasury's financing plans. In the present circumstances, he would adhere as closely as possible to the policy that had been followed while doing as much in the way of further ease as could be done in the circumstances.

Mr. Shepardson made several comments on the agricultural situation in the light of his attendance at the recent fall meeting of the National Agricultural Credit Committee. He noted, first, that the level of land prices appeared definitely to be trending downward. In some districts there had been no appreciable change as yet, but in other districts prices had fallen as much as 2 or 3 per cent, and for the country as a whole they were down almost 2 per cent. In a few areas, particularly in the corn belt, there had been a very perceptible drop. Second, all areas reported almost a complete lack of city buyers for farm property.

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A constantly increasing percentage of farm purchases was for enlargement of existing units, and there was little in the way of entry of new farm owners. Third, the rate of expansion of farm mortgage debt was down significantly and the rate of expansion of other debt had slowed considerably, with a particular reaction in the amount of feeder loans. There had been some increase in delinquencies and in foreclosures, the latter representing mostly a closing out of inefficient operators. As previously indicated at the spring meeting of the same group, it appeared that more attention was being given to the earning capacity of the borrower and that less reliance was being placed on the security for the loan. Reports from the Department of Agriculture on farm income indicated that while there was some slackening in farm prices there had also been a slackening in farm costs, so the net return to farmers was anticipated to be fully as good or possibly a little better than last year.

Turning to the general economic situation, Mr. Shepardson noted the diversity of indicators and trends. He was not sure that the balance-of-payments picture could be changed fast, one reason being that price adjustments do not come about quickly. The report on the price situation was encouraging to him for it appeared that more and more sharp-pencil adjustments were taking place; although list prices had not changed much, deals were being made. He felt that those adjustments were wholesome and that they had to occur if there was going to be an improvement in the balance of current accounts. He did not feel that

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the situation with respect to the movement of capital or the expenditures of Government would change fast, but he hoped that there might be somewhat greater scrutiny of expenditures and appropriate restrictions placed upon the use of funds.

Mr. Shepardson said he thought the unemployment situation was going to be relieved only as demand, not the credit situation, improved. He did not feel that the slack at the moment was due to a lack of credit but rather to a lack of demand at existing prices.

Mr. Shepardson expressed the view that the System had followed a good program recently and that the results had been satisfactory. He thought the Committee should continue to maintain about the degree of ease that had prevailed and that reserves needed for seasonal purposes should be supplied willingly. However, he questioned whether reserves should be pressed on the market at this time. The time might be approaching, if it was not already here, when in order to try to maintain a given level of free reserves the Committee would have to keep pressing to the point where there might be a recurrence of the situation that prevailed a couple of years ago. For that reason he would align himself with the views of Messrs. Leach, Irons, and Deming. He would supply needed reserves and maintain an even keel, but he would not press reserves on the market. If free reserves, on average, fell from the \$480 million figure indicated by the projections to \$400 million or even \$350 million, he did not think that that would be serious.

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Mr. King said that he would recommend no change in the discount rate or in the directive, which left for consideration the matter of instructions to the Desk. Before coming to that, however, he wished to make a comment on the price adjustments that were being mentioned. In his opinion they did not offer real hope for long-range adjustment because they were based on a desperate need to move goods rather than a reduction in manufacturing costs. Therefore, he got little comfort from the fact that some such price adjustments apparently were taking place. While they might afford a little relief to the general economy, he doubted whether they would provide any long-range correction of the basic problem.

As he understood the discussion, Mr. King said, the Committee was in practically unanimous agreement that the atmosphere that had prevailed in the market should continue to prevail. It also seemed to be fairly well agreed that it would not be desirable for bill rates to go lower. Accordingly, the Account Manager might find himself in a difficult position, and it seemed appropriate to provide some guidance if the Manager should find that the conflicting objectives produced an impossible situation. Personally, he considered it more important not to let short-term rates go substantially lower than to maintain the prevailing atmosphere of ease in the market. He was doubtful as to whether that ease was really accomplishing very much, while he was fairly

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well convinced that it would be undesirable for short-term rates to go lower. Therefore, if it became necessary to supply additional reserves in large quantity, he would consider the possibility of using other maturities, although he realized that this might ultimately affect short-term rates. If the present policy could not be pursued without affecting short-term rates unduly, he felt that the Board perhaps should consider taking action through some means other than open market operations.

Mr. Fulton reported that the trend in the Fourth District was slightly downward. Department store sales had not come up to expectations and insured unemployment was up in some areas, particularly the steel-producing centers. In other places, however, there had been some improvement in the unemployment situation due to the new model automobiles going into production. The steel industry seemed to be living on hopes, and the operating rate this week would be below last week. Although there had been some pickup in orders, the pickup was slight, and nobody in the steel industry to whom he had spoken looked for any marked rise.

Mr. Fulton said that the auto companies were doing about as well as had been expected, except that Chrysler had cut back production because of the large number of cars produced in the past few weeks. Orders were being placed quite cautiously, with full knowledge of the large overhang of unsold 1960 models. Were it not for the auto companies, however, the steel mills would be in bad shape because orders from other users had been declining. There were practically no orders for transmission

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pipe and bars. Tin plate was also moving slowly; the can manufacturers had experienced a cutback in orders because the cool summer had delayed some crops. For this reason also, beer and soft drink cans had not been so much in demand. There was no forward buying of steel and orders were for immediate delivery, so the mills were forced to inventory for immediate delivery. It appeared that about 5 million tons of foreign steel would come in this year, and while exports of steel had increased, they were not going to reach 5 million tons. Projections for production in the fourth quarter were slightly above present levels and there did not seem to be too much joy in the outlook for next year, the forecast being that production would be about the same as this year, at least until about the fourth quarter. If current projections for this year were realized, production would probably amount to somewhat less than 105 million tons. Profits were being hurt, with some companies in the red and likely to wind up in the red for this year. Contractual wage increases in December would tighten the profit squeeze further unless prices could be raised, which seemed highly unlikely.

As to the machine tool industry, Mr. Fulton said that after the recent exposition in Chicago some good orders, both domestic and foreign, had been received. One machine toolmaker had expressed the view that the industry was becoming quite competitive and therefore was getting orders for some of the smaller machines not previously sold abroad to any extent.

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Mr. Fulton said that he would not favor reducing the discount rate or changing the policy directive, and that he thought the Desk had done a good job in the past three weeks. He would like to see the same degree of ease maintained, with emphasis not on free reserves but on the feel of the market, the level of short-term rates, and the Federal funds rate, since in his opinion these were the things that were most indicative of the condition of the market. He concurred in the view of Mr. Treiber that a reduction in margin requirements would do no violence at the present time and might be of help to the stock market from a psychological standpoint.

Mr. Bopp stated that conditions in the Third District were approximately the same as in the country as a whole. In brief, developments had been disappointing. A recent survey of housing and the real estate market reflected considerable pessimism, and at a recent meeting of the Philadelphia Economists' Discussion Group the views were almost unanimously gloomy regarding the remainder of 1960 and most of 1961. The gloom was not deep but it was widespread, and there were few exceptions.

Mr. Bopp went on to say that there had been a significant increase in bank loans and investments, and also in deposits, which was encouraging in terms of what the Committee had been trying to do recently. One bright spot was that the operating rate in steel had improved, although the improvement was only to 62 per cent of capacity.

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As to policy, Mr. Eopp said he was concerned about the sluggishness in the capital markets, where developments seemed somewhat similar to 1958. Although, for a variety of reasons, he felt that nothing should be done at this point, the movement of ease from short-term to long-term markets is not always as automatic as one might hope. He would keep reserve positions in continued ease and would hope that the Federal funds rate might be fairly frequently below the discount rate. However, this was qualified by realization that the Account Manager would have to walk a tight rope so that short-term rates would not be pushed lower. He would recommend no change in the discount rate or in the directive at this time.

Mr. Patterson said that in August additional signs of weakness in economic activity and available comparisons indicated that Sixth District activity was no better and might be somewhat weaker. In that month nonfarm employment declined in all States of the District except Tennessee, where a slight rise occurred. Manufacturing employment, however, had not declined quite as much as in the nation as a whole. Cotton textile activity had weakened considerably in recent months, with seasonally adjusted cotton consumption in August about 6 per cent below January. This had affected Georgia particularly because of the relative importance of textile manufacturing there, and to a lesser extent Alabama and Tennessee.

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Sixth District retail spending had been sluggish, Mr. Patterson said, just as in the nation. Department store sales, which had been showing greater strength than nationally, dropped 8 per cent in August compared with a national decline of 3 per cent. In September, District department store sales were unchanged. Bank debits, although up in August, had been trending downward somewhat more in the District since February than in the nation. The sales picture within the District had been spotty, with none of the States as a whole showing either general weakness or strength. Automobile sales were apparently doing better than in the nation, judging from registration figures through July. For the first seven months, registrations in District States were nearly 10 per cent above the comparable period of last year compared with a national gain of just over 8 per cent.

Continuing, Mr. Patterson said that residential building had been somewhat stronger in the District than in the nation, although activity in Alabama, Louisiana, and Florida was off sharply from a year ago. Mortgage funds were becoming more plentiful, but easier money had not yet resulted in the hoped-for upturn in residential construction. The District's farm economy, although showing mixed trends, had not weakened materially in recent weeks except in Florida, where citrus and vegetable crops were damaged by hurricane Donna. Loans and investments at banks in leading District cities increased substantially during the first three weeks in September, showing response to System actions.

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Mr. Szymczak said that in light of the uncertainties that existed and would continue to exist, he thought that monetary policy had done a good job and that the present policy should be continued. He felt that the Manager of the System Open Market Account had done an excellent job in the market and that the Committee should continue to pursue the policy it had been following. He would favor deferment of any change in margin requirements or in reserve requirements at either central reserve city or country banks.

Mr. Balderston said he was comforted by the fact that at long last the money supply seemed to have responded to monetary policy and by the fact that the seasonally adjusted money supply has risen about one billion dollars between June and the middle of September. A related fact was that turnover outside the financial centers was as high as in June and some 7.5 per cent higher than a year ago.

Mr. Balderston said he shared the view expressed by many today that the economy had turned downward and that it was following the traditional course that was to be expected. If one looked at Shiskin's business cycle series, which is more broadly based than the series contained in publications of the National Bureau of Economic Research, he would find now that even some of the laggards were beginning to turn down. This was to be expected at this stage of the business cycle; it would be unusual if any upsurge were to grow out of the present situation.

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Therefore, Mr. Balderston said, he concluded that the System had been correct in taking action early. However, he felt that the System should not press its luck until the effects of what had already been done could be observed. The money supply appeared to be responding, and it would seem advisable to wait and see how great the response might be.

Mr. Balderston said he would suggest a target of free reserves of about \$400 million, realizing that the Committee had been on this target since about the first of September and that experience had demonstrated that there is a cumulative effect in keeping the same target week after week and month after month.

Chairman Martin said he thought System policy had been effective and that it was a good policy. He wished only to emphasize the point that had been made that the Account Manager should operate on the feel and tone of the market and not the statistics. The dead hand of statistics had been responsible for many of the System's difficulties.

After commenting that monetary policy could not seek to correct all of the problems of the world, Chairman Martin said he continued to feel more hopeful about the economy, from a long-range standpoint, than a year ago. A year ago he saw no answers to some of these problems, but today he thought the answers were coming in the rolling adjustments that were being made. Whether we as a people had the courage, intelligence, and capacity to accept them was another matter. However, he continued to have a feeling that the nation did have that capacity.

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Chairman Martin said that the consensus today seemed clear. There should be no change in policy, in the directive, or in the discount rate. Also, it had been suggested that the Board consider certain questions that were within its jurisdiction.

In reply to a question by the Chairman, Mr. Rouse said that he had no comments.

The Chairman then inquired whether others had anything further that they would like to say, and no comments were heard.

Thereupon, upon motion duly made and seconded, it was voted unanimously 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 encouraging monetary expansion for the purpose of fostering sustainable growth in economic activity and employment, 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

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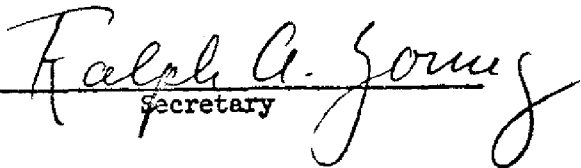
amounts of special short-term certificates of indebtedness as may be necessary from time to time for the temporary accommodation of the Treasury; provided that the total amount of such certificates held at any one time by the Federal Reserve Banks shall not exceed in the aggregate \$500 million.

Chairman Martin noted that pursuant to the understanding at the meeting on September 13, 1960, there appeared on the agenda for this meeting further discussion of the memorandum from the Federal Reserve Bank of New York dated September 8, 1960, recommending that the Bank's Market Statistics Department be authorized to furnish to the Securities Department quarterly statistics on the trading volume of individual Government securities dealers. If there was no objection, however, he would like to hold this topic over until another meeting. Two Committee members and one other President were absent today, and he was quite sure that one of them, at least, would like to comment on the matter.

No objection to Chairman Martin's suggestion was indicated.

It was agreed that the next meeting of the Federal Open Market Committee would be held in Washington on Tuesday, October 25, 1960, at 10:00 a.m., and that succeeding meetings of the Committee would be scheduled tentatively for November 22, 1960, and December 13, 1960.

The meeting then adjourned.


Secretary