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ANNUAL REPORT

of the

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

COVERING OPERATIONS FOR THE YEAR

1957

Digest of Principal Federal Reserve Policy Actions, 1957

Period	Action	Purpose of action
January–June	Reduced holding of U. S. Government securities by about $1.8 billion. Member bank borrowings increased from an average of $400 million in January to $1 billion in June.	To offset the effect on reserves of seasonal factors and the sale of $600 million of gold to the United States Treasury by the International Monetary Fund, and to exert pressure on bank reserve positions by bringing about a higher level of member bank borrowings.
August	Raised discount rates from 3 to 3½ per cent at all Reserve Banks.	To bring discount rates into closer alignment with open market money rates and maintain the restrictive effect of member bank borrowing.
July–Mid-October	Bought and subsequently sold small amounts of U. S. Government securities at various times. Member bank borrowings remained at or near average of $1 billion.	To meet changing reserve needs and at the same time maintain continuing pressure on bank reserve positions.
Mid-October–December	System holdings of U. S. Government securities increased by $1 billion, including substantial amounts of securities held under repurchase agreement. Member bank borrowings declined to an average of less than $750 million.	To increase the availability of bank reserves and thereby cushion adjustments and mitigate recessionary tendencies in the economy.
November–December	Reduced discount rates from 3½ to 3 per cent at all Reserve Banks.	To reduce the cost of borrowing from the Reserve Banks and eliminate any undue restraint on bank borrowing in view of the decline in business activity and evidences of economic recession.

RECORD OF POLICY ACTIONS
FEDERAL OPEN MARKET COMMITTEE

The policy directive of the Federal Open Market Committee in effect at the beginning of 1957 was the directive that had been approved at the meetings on November 27 and December 10, 1956. This directive, which placed emphasis on restraining inflationary developments and which was issued to the Federal Reserve Bank of New York as the Bank selected by the Committee to execute transactions for the System open market account, read as follows:

(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 developments in the interest of sustainable economic growth, while recognizing additional pressures in the money, credit, and capital markets resulting from seasonal factors and international conditions, 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;

(3) To sell direct to the Treasury from the System account for gold certificates such amounts of Treasury securities maturing within one year as may be necessary from time to time for the accommodation of the Treasury; provided that the total amount of such securities so sold shall not exceed in the aggregate $500 million face amount, and such sales shall be made as nearly as may be practicable at the prices currently quoted in the open market.

employment in October had receded further from the peak reached in August. Not only were the signs of domestic decline fairly general, but in Canada recession tendencies had become clear, and in Europe industrial activity which had ceased expanding in late spring of 1957 had tapered off moderately through the summer months.

Although the Committee's analysis showed that the domestic economy still was operating at high levels and that the downward adjustment thus far had been moderate, there no longer was much doubt that at least a mild downturn in business activity was under way, and there was widespread belief that it would probably continue well into 1958. The major question seemed to be not whether a further business decline would occur, but for how long and in what degree. In terms of credit policy, the question presented was how far the Committee should go at this time in recognizing the change in the economic situation and outlook, and by what means.

The Committee's decision at this meeting was that action should now be taken to recognize the change in the general economic situation away from the sidewise movement that had prevailed during most of 1957. This did not signify a shift that would entirely eliminate restraint on credit expansion, but it did reflect a decision that there should be a moderate relaxation of the degree of restrictive pressure. It was on the basis of this general view that the directive was changed to eliminate the previous clause (b) which had called for restraining inflationary pressures and to replace that clause with wording that provided for open market operations with a view, among other things, "to fostering sustainable growth in the economy without inflation, by moderating the pressures on bank reserves."

Mr. Robertson dissented from the foregoing action with respect to the insertion in clause (b) of the words "by moderating the pressures on bank reserves." His action was based on the belief that the prevailing condition of the economy was not such as to call for a lessening of restraint, that inflationary potentials were still strong, and that continued restraint was essential to their containment.

There was also a discussion at this Open Market Committee meeting, at which all of the Federal Reserve Bank Presidents were in attendance, of the relationship of open market policy to the discount rates of the Federal Reserve Banks and the appropriateness of those rates in view of the changed economic situation and the change in open market policy.

December 3, 1957

1. Authority to effect transactions in System account.

The Committee renewed its directive in the same form that had been adopted at the meeting on November 12, 1957, at which time the wording of clause (b) of the first paragraph had been changed so that it called for operations in the open market with a view, among other things, "to fostering sustainable growth in the economy without inflation, by moderating the pressures on bank reserves."

> Votes for this action: Messrs. Martin, Chairman, Hayes, Vice Chairman, Allen, Balderston, Bryan, Leedy, Mills, Shepardson, Vardaman, and Williams. Vote against this action: Mr. Robertson.

The economic report at this meeting was consistent with that presented at the meeting on November 12 showing a moderate downsettling of the economy. Industrial production had continued to sag, especially in the areas of steel and other metals, equipment and ordnance, household durables, apparel and textiles, and mining, but higher automobile output had tended in the direction of maintaining the level of the index of industrial production. On the other hand, new construction was being well maintained, with residential and public utility construction up, industrial construction down, and commercial and public construction about even.

The further sag in equipment production and industrial construction was closely related to cutbacks in spending decisions for business, plant, and equipment. Information that had just become available on third quarter capital appropriations of large manufacturing companies showed a decline of almost a third from a year earlier. This was the second successive quarter showing a substantial decline. Labor market data showed a further rise in unemployment claims, with increases fairly widespread geographically. The mid-November unemployment survey showed substantially more than the usual seasonal rise in number of unemployed to a seasonally adjusted level of about 5.2 per cent of the labor force. Gross national product for the fourth quarter of the year according to preliminary estimates would probably show little change or moderate decline from the third quarter of the year. Personal income in October had declined for the second successive month due to reduced wage and salary disbursements. The general average of wholesale prices had shown little change in November, while the consumer price index which was unchanged in October was expected to show a rise in November, reflecting higher new automobile prices and additional advances in rents and service costs.

In the credit field, cross currents in economic forces in recent weeks had precipitated sharp and often paradoxical developments in financial markets. Through action reducing the discount rates of the Federal Reserve Banks from a 3½ per cent level to a 3 per cent level in mid-November, there had been public recognition by the Federal Reserve System that economic adjustment had lessened and perhaps removed the threat of inflation for the time being. Prices of securities in the stock market had increased sharply in this period, and prices of bonds had risen substantially with corresponding decreases in yields. Bank credit had continued to decline, contrary to the usual seasonal tendency at this time of year.

As a result of the slackened growth in bank credit and deposits, required reserves of member banks had failed to show the customary seasonal increase in November. In addition, reserves had been supplied by a reduction in Treasury balances at the Federal Reserve Banks and by substantial System purchases of bills. The cumulative results of these measures were being reflected in member bank reserve positions at the time of this meeting, and it was expected that if the Treasury continued to keep its balances in the Federal Reserve Banks at a low level, no strain on member bank positions would occur during December despite customary seasonal demands for additional funds.

In the Committee's review of the economic situation, the view was advanced that while it had become more evident than at earlier meetings that business was declining, there were basic uncertainties that made it difficult to assume either a prompt resumption of the upward movement in business or much further continuation of the decline. In these circumstances, the general view of the Committee was that there should be further moderating of the restrictive pressures on credit expansion and, for this reason, the directive was renewed with the same terms that had been approved at the meeting on November 12 calling for "fostering sustainable growth in the economy without inflation, by moderating the pressures on bank reserves."

Mr. Robertson dissented from this action for the same reasons as those stated previously for dissenting from the wording adopted at the meeting on November 12.

2. Rate of interest on special certificates.

The Committee authorized that the rate to be charged on special short-term certificates of indebtedness purchased direct from the Treasury pursuant to paragraph (2) of the Committee's directive to the Federal Reserve Bank of New York be fixed at one-fourth of one per cent below the discount rate of the Federal Reserve Bank of New York at the time of such purchase.

> Votes for this action: Messrs. Martin, Chairman, Hayes, Vice Chairman, Allen, Balderston, Bryan, Leedy, Mills, Shepardson, and Vardaman. Votes against this action: Messrs. Robertson and Williams.

Section 14(b) of the Federal Reserve Act authorizes purchases or sales of securities by the Federal Reserve Banks direct from the United States Treasury under certain conditions and with a proviso that the aggregate amount held by the Reserve Banks at one time shall not exceed $5 billion. Paragraph (2) of the Committee's directive, which authorized purchases for the account of the Federal Reserve Bank of New York of such amounts of special short-term certificates of indebtedness as may be necessary from time to time for the temporary accommodation of the Treasury, had been used infrequently over the years and had not been used at any time since March 1954. The rate charged for the facility when it had been used had been one-fourth of one per cent, a rate that had prevailed since the early 1940's when the discount rates at the Federal Reserve Banks were at the one-half per cent level.

The purpose of the Committee in taking the action was to adopt a procedure which would provide for a rate that was flexible and closer to the current market.

In voting against this action, Messrs. Robertson and Williams indicated that they felt the matter was of little importance and that on the whole it would be preferable to let the existing rate of one-fourth of one per cent stand.