

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, May 5, 1964, at 9:30 a.m.

PRESENT: Mr. Martin, Chairman^{1/}
Mr. Balderston
Mr. Daane
Mr. Hickman
Mr. Mills
Mr. Mitchell
Mr. Robertson
Mr. Shepardson
Mr. Shuford
Mr. Swan
Mr. Wayne
Mr. Treiber, Alternate for Mr. Hayes

Messrs. Ellis, Scanlon, and Deming, Alternate Members of the Federal Open Market Committee

Messrs. Bopp, Clay, and Irons, Presidents of the Federal Reserve Banks of Philadelphia, Kansas City, and Dallas, respectively

Mr. Young, Secretary
Mr. Sherman, Assistant Secretary
Mr. Broida, Assistant Secretary
Mr. Hackley, General Counsel
Mr. Noyes, Economist
Messrs. Brill, Garvy, Grove, Holland, Jones, Koch, and Mann, Associate Economists
Mr. Stone, Manager, System Open Market Account
Mr. Coombs, Special Manager, System Open Market Account

Mr. Molony, Assistant to the Board of Governors
Mr. Cardon, Legislative Counsel, Board of Governors

Messrs. Partee and Williams, Advisers, Division of Research and Statistics, Board of Governors
Mr. Wood, Associate Adviser, Division of International Finance, Board of Governors

^{1/} Left the meeting at the point indicated.

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Mr. Axilrod, Chief, Government Finance
Section, Division of Research and
Statistics, Board of Governors
Miss Eaton, General Assistant, Office of the
Secretary, Board of Governors

Messrs. Heflin and Patterson, First Vice
Presidents of the Federal Reserve Banks
of Richmond and Atlanta, respectively

Messrs. Taylor, Baughman, Parsons, Tow, and
Green, Vice Presidents of the Federal
Reserve Banks of Atlanta, Chicago,
Minneapolis, Kansas City, and Dallas,
respectively

Mr. Sternlight, Assistant Vice President,
Federal Reserve Bank of New York

Mr. Anderson, Financial Economist, Federal
Reserve Bank of Boston

Mr. Rothwell, Economist, Federal Reserve Bank
of Philadelphia

Before this meeting there had been distributed to the members of the Committee a report from the Manager of the System Open Market Account covering open market operations in U. S. Government securities and bankers' acceptances for the period April 14 through April 29, 1964, and a supplemental report covering the period April 30 through May 4, 1964. Copies of these reports have been placed in the files of the Committee.

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

The climate of reserve availability during the period since the last meeting has remained within the range of variation established during the past several months. Federal funds have traded in good volume and mainly at 3-1/2 per cent, although dipping slightly lower on a few days. Member bank borrowing was largely within a daily range of about \$100 to \$400 million, although it climbed higher on occasion--most notably on Wednesday, April 15, a double settlement date which was complicated by large flows of funds in connection with the Treasury's paydown of \$2-1/2 billion of maturing bills. In order to make that outpayment, the Treasury made heavy special calls on its major commercial bank depositaries (the "C" banks) and this tended to concentrate reserve pressures on the central money market. The money market continued quite firm through April 17 as the Treasury made additional special calls on the "C" banks to cover net cash outflows.

After the 17th, however, the pressures on the central money market began to abate--particularly after April 22 when the Treasury began to redeposit the earlier special calls on the "C" banks and made further net redeposits with those banks. Over the 10-day period from April 22 to May 1 the redeposit of earlier calls plus further net deposits to the "C" banks came to more than \$2 billion. This situation came about as heavy individual income tax receipts flowed into the Treasury's account at the Reserve Banks; to keep member banks reserves from being absorbed through this process, it was necessary to make the large redeposits to the "C" banks. Yesterday, it was possible to begin reversing the heavy net redeposits with the "C" banks and this should help to restore the position of basic reserve deficiency under which many of the large money market banks, particularly those in New York, typically operate.

In the Treasury bill market rates edged gradually lower through most of the past three-week period--largely in reflection of vigorous demand growing out of investment of some State and local tax receipts and reinvestment of the proceeds of the Treasury's April 15 bill maturity. These demands encountered market supplies that were already depleted through factors operating in March and early April--such as the reinvestment of the telephone company's stock sale proceeds. Investor demand was augmented by increased dealer demand as the dealers sought to rebuild inventories in anticipation of a Treasury exchange offering in which

selling of "rights" would generate demand for bills. At their low point, the three-month bill dipped to about 3.45 per cent while the six-month issue declined to 3.59 per cent compared with rates of about 3.50 and 3.70 per cent at the start of the period.

In the last few days a more cautious atmosphere has developed in the bill market and rates have inched a little higher despite the very substantial purchases by the Open Market Account to offset month-end reserve drains. In part, the heavier tone seems to have resulted from a smaller than expected demand for bills coming out of selling of refunding "rights." In the bill auction yesterday, average issuing rates were set at about 3.48 and 3.63 per cent for the three- and six-month bills, respectively, about unchanged and down 6 basis points from the rates three weeks earlier.

In the Treasury bond market the center of attention has been the anticipation of, and reaction to, the Treasury's May exchange offering. Through most of the recent period the market awaited the Treasury's offering in an atmosphere of growing confidence in current rate levels, following the uneasy period and price markdowns that occurred through most of March. Heartened by the improving market atmosphere, the Treasury offered a 10-year 4-1/4 per cent bond at par in addition to a widely anticipated 18-month note, and the offering is being very well received. There has been a particularly strong interest in the 10-year 4-1/4's--an offering that would have seemed quite unpalatable a scant few weeks ago. Relatively few maturing "rights" have been coming into the market, with the result that at the close last night, the new 4-1/4 per cent bonds were bid at about 100-1/4 in when-issued trading, while the various "rights" issues carried comparable premiums. Interest in the 4 per cent notes is moderate in comparison, but it is expected that a good many rights holders will choose to exchange for the shorter issue. I should add in this connection that the System holds approximately \$6.3 billion of the maturing May 15 issues and we plan to exchange these for the 18-month 4 per cent note.

The corporate and municipal bond markets were also steady and quiet while awaiting the Treasury's refunding terms. New issues were fairly well received although no great enthusiasm developed. Thus, the \$100 million telephone issue offered during the period was some 70 per cent sold

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the first day but subsequent progress was slow and yesterday the remaining quarter of the issue was released from syndicate with a modest upward yield adjustment of 3 basis points (to 4.51 per cent).

In response to questions, Mr. Stone commented that it was difficult to say whether the sizable premiums at which rights were trading would lead to problems in the aftermarket, but he felt the situation might be healthier if the premiums came down somewhat before the books closed on Wednesday. Attrition was expected to be larger than usual in this exchange. Some market observers were guessing that exchanges would be made into the two issues in about equal amounts, but others thought that somewhat more than half would be made into the 18-month notes. There appeared to be little or no speculative interest in the 4-1/4 per cent bond.

Thereupon, upon motion duly made and seconded, and by unanimous vote, the open market transactions in Government securities and bankers' acceptances during the period April 14 through May 4, 1964, were approved, ratified and confirmed.

Chairman Martin then called for the staff economic and financial reports, supplementing the written reports that had been distributed prior to the meeting, copies of which have been placed in the files of the Committee.

Mr. Koch presented a statement on economic conditions as follows:

Most of the business and economic news that has become available since our last meeting has been consistent with the

course of developments the staff has been sketching out at these meetings for some time now, namely, a moderate and relatively well balanced economic expansion. Industrial production was probably up a little more in April and employment rose further, but the rate of unemployment continued around 5-1/2 per cent. Preliminary March and revised February inventory figures suggest that accumulation of stocks was even less in the first quarter than had been thought earlier.

Both the leading and coincident economic indicators continue strong, an unusual development for a business cycle over three years old. The leading indicators generally become weak several months before general business.

The evidence is still by no means all in on the initial effects of the tax cut in stimulating spending, but thus far they seem to have been mild. Total retail sales in March were down from those in February, and thus far in April they appear to be down a little further. Whether this recent behavior of consumer spending can be fully explained by such factors as cool and rainy weather and the early date of Easter is doubtful. A more satisfactory explanation seems to be that the tax cut was in part anticipated by consumers, thereby contributing to the heavy retail sales and consumer credit extensions during the winter, and in part that the cut has lagged spending effects. A recent econometric study, for example, suggests that spending response in the first quarter following the cut may be less than half of the eventual over-all spending impact. Moreover, some individuals are increasing their tax withholdings, thereby temporarily increasing their savings. In any case, it is now evident that the cut has not created an immediate buying spree on the part of consumers.

The economic news that has probably received the most widespread comment during the past three weeks has been the new McGraw-Hill survey of anticipated plant and equipment spending by business concerns in 1964. The 12 per cent increase in such spending over 1963 suggested by the new survey is not significantly different from the 10 per cent estimated rise obtained in the Commerce-SEC survey taken in February. The McGraw-Hill data are more heavily weighted by the larger corporations which are apparently engaging in heavier capital expansion programs than smaller ones.

The revised McGraw-Hill survey does not suggest an investment boom this year. Nor do recent data on new orders for durable goods, which are down from their January peak. Using the McGraw-Hill anticipation figures, business plant

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and equipment spending on a constant dollar basis would total only 6.8 per cent of a projected GNP of \$625 billion this year, as compared with 7.8 per cent in 1957. Thus, the rate of investment does not as yet appear to be getting out of line with consumption.

It must also be remembered that business capital spending adds after a time to the capacity to produce goods and services although the initial effect is to add to the aggregate demand for such goods and services. In the new survey, McGraw-Hill notes that for the first time in several years businesses are increasing somewhat the proportion of their total capital spending that provides new capacity, as contrasted to that which modernizes and improves existing capacity. The increase in total manufacturing capacity estimated to be achieved in 1964 is about 5 per cent. Thus, if McGraw-Hill's estimated sales increase of 6 per cent in 1964 is achieved, the rate of utilization of manufacturing capacity would only be a little higher at the end of the year than the 35-87 per cent rate estimated for the beginning.

As for the strategic area of prices, decreases as well as increases have appeared in the news recently, but with the increases still more frequent. Decreases, however, have occurred in meats, petroleum, textiles--reflecting the reduced cotton prices for domestic producers--and selected steel products, reflecting import competition. On balance, since the beginning of the year most of the broad general price indices have changed little.

As for the labor area, there has been no change in hourly earnings in manufacturing in recent months and productivity is still apparently continuing to rise. As a result of these developments, unit labor costs in manufacturing are no higher than a year ago and below the 1957-59 average.

Greater volume, firm prices, and steady labor costs have resulted in sharply higher corporate profits. A preliminary estimate of manufacturing profits after taxes in the first quarter of 1964 showed an increase of 23 per cent over the comparable period a year ago. Moreover, a dollar of corporate profits today no doubt means more for the stockholder than the same amount some years ago both because it contains relatively little erratic inventory profits and because it is computed after more generous allowances for depreciation and obsolescence of facilities.

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These higher current corporate profit figures have no doubt been discounted in part by the stock market where, even though common stock prices have fluctuated rather widely recently, they remain 7 per cent above their level at the beginning of the year and 10 per cent above their earlier peak in December 1961.

To sum up, my reaction to current domestic economic developments is that they are reassuring and not yet suggestive of a speculative boom. The expansion continues moderate and the response of consumers and businesses to the tax cut has been cautious and exploratory. There is as yet little evidence that either capacity limitations or an unsustainably rapid rate of increase in over-all demand threatens the expansion's sustainability.

Mr. Brill made the following statement concerning financial developments:

The lack of ebullience that seems to characterize non-financial areas of the economy carries over to most financial markets as well. Earlier this year there was a widely-held conviction in the financial community that interest rates would move up promptly after enactment of the tax cut, partly as a result of surging credit demands and partly as a result of monetary policy actions. Neither has transpired. Credit expansion, at least bank credit growth, seems to have moderated in recent weeks, and the market isn't able to read any policy move toward restraint into recent fluctuations in the free reserve figures. Market convictions, therefore, seem to be shifting to the other extreme. Some investors were shortening portfolio positions earlier in March; many are now apparently anxious to acquire the 10-year bond offered by the Treasury last week, rights to which have gone to a 7/32 premium.

It is tempting to say that the market is as wrong now as it was two months ago, but the evidence isn't all that clear. Investors could be right in behaving as though the peak of upward pressure on interest rates has passed. Nevertheless, there are some alternative explanations for recent developments that leave the future course of credit flows and interest rate pressures as murky as ever.

In long-term markets we have been getting a pattern of saving and borrowing flows reminiscent of earlier postwar upswings: large demands on capital markets, a leveling off and perhaps a decline in the flow of savings to financial intermediaries, an increase in direct investment in market

instruments and, until recently, an upward drift in long-term rates. Security flotations by corporations and State and local governments were as large in the first quarter of the year as in the comparable months of the past two years, and mortgage debt expansion was one-tenth larger than the rate a year ago.

Or the other hand, the inflow of savings to major financial institutions has continued to run well below the pace of early 1963. Savings and loan associations were hard hit in January and, although inflows recovered some in February and March, the total for the first quarter was one-fourth less than a year ago. Mutual savings banks inflows were exceptionally large in January, following a ceiling rate adjustment in New York, but by March inflows were lagging the 1963 pace. Commercial bank time and savings deposits continued to expand rapidly through January, but in February and March the rate of growth dropped sharply. In light of these reduced saving flows but continued large credit demands, and in light of the expectations prevailing through most of the period, it is surprising that the rise in long-term rates from the end of the year through March was as mild as that which actually occurred--about one-eighth of a per cent on new corporate issues and less than that of seasoned corporates and municipals and long-term Governments.

Since April, long-term rate pressures appear to have receded. The turn-about is hard to explain in terms of what little we know of saving and borrowing flows. Corporate and municipal security financing was in near record volume for the month, with the AT&T issue and several large municipal flotations hitting the market. While inflows picked up somewhat at commercial banks in the second half of April, the gain for the month as a whole in time and savings deposits was not dramatic. We have no data for April on other institutions, but there has been no indication to suggest a resumption of large savings inflows. In fact, payments for the AT&T issue may have resulted in some decline. The moderate easing in long-term rates that has occurred since March, then, must be chalked up to shifts in investor attitudes rather than to any observable change in the balance of long-term credit demand and supply.

The easing that has occurred in short-term rates has somewhat more foundation in fund-flow relationships, although it also has reflected some shift in market expectations. On the supply of funds side, corporations have been in better

position to add to their holdings of liquid financial assets. The margin of retained earnings and charges over actual expenditures for fixed capital and inventories remained high in the first quarter, while at the same time corporations were floating a large volume of securities, proceeds for which were apparently not needed for immediate disbursement. Commercial banks also added to the supply of funds for short-term investment as they shortened portfolios in March in preparation for business loan demands, but these as yet have not materialized to the extent anticipated.

On the demands for funds side, the Treasury has not been adding to the net supply of bills in its weekly auctions. In the first four months of this year the Treasury just rolled-over all maturing issues. In the comparable period last year, the Treasury raised new cash in seven of the weekly auctions, thereby adding \$1 billion to the total of bills outstanding. In 1962 they raised new cash in 12 weekly auctions during the January-April period, adding \$1.2 billion to the supply of outstanding bills.

With earlier years' experience as background, the market kept expecting similar developments this year, particularly after the British Bank rate was raised. But when the British action was not followed by action on our discount rate, and when the volume of maturing bills dropped from \$2.2 to \$2.1 billion in the early part of April and the Treasury let the new auction drop to the lower level, the market took this as a signal that official policy was changing to permit more flexibility in short-term rates.

This new market conviction was reinforced by the results of System operations. Free reserves since late March have generally run above the February and March averages, with borrowing generally much lower, and there has been somewhat less tautness in the Federal funds market. The flow of Federal funds has been quite large, and the rate on funds has been below the discount rate quite a bit more frequently than earlier this year.

Developments in short-term markets can be summarized as follows: seasonal downward pressures on bill rates have been accentuated by exceptional corporate affluence and by commercial bank portfolio positioning and, for the first time since 1961, the Treasury and the System have allowed these seasonal, and to some extent cyclical, pressures to be reflected, at least partially, in short-term rates.

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What does this all add up to as far as clues to the economy's performance and to the appropriate posture for policy? The recent easing in long- and short-term rates does not suggest any fundamental change in basic financial forces, despite the shifts in investor expectations. There is no reason, from the evidence to date, to suspect that continued economic expansion and normal seasonal developments won't begin to bring upward pressure on the rate structure by mid-year, and perhaps earlier if the Treasury decides to anticipate some of its second-half financing needs or if the market begins to feel it has over-shifted on expectations.

Whether it will be appropriate to let these upward pressures be reflected in the market will depend on the state of the economy at that time. For the present, with a moderate and orderly expansion going on in the nonfinancial arena, there doesn't seem to be any domestic reason for the System to fight this return to more normal seasonal rate patterns. There is certainly nothing in the picture of sufficient urgency to suggest a departure at this time from traditional "even-keeling" during the Treasury's financing.

Mr. Wood presented a statement on the balance of payments as follows:

In April, the U.S. payments balance reverted to a large deficit, perhaps in the range of \$300 to \$400 million, according to the tentative weekly data. It seems, however, that this deficit reflected mainly or exclusively an outflow of liquid funds to Canada, offsetting a similar inflow in March. Thus, the change from March to April may have been a new kind of seasonal movement, perhaps in part connected with the Illinois State property tax, which already bedevils statistics on domestic money supply. Illinois corporations have become accustomed to investing about \$100 million of their liquid funds in Canada; they may have converted these assets temporarily into tax-exempt U.S. Treasury bills over the first-of-April tax date, just as they do with their U.S. deposits.

Interpretation of the April deficit as reflecting to a large extent financial movement of volatile funds is supported by the fact that U.S. monetary reserves remained unchanged, with an increase in U.S. gold holdings of \$175 million offset by a similar decline in official holdings of foreign convertible currencies. Liabilities to foreign official holders

apparently declined further, according to the tentative weekly data; but this decline reflected at least in part the "swaps" between the Bundesbank and the German commercial banks, which have been reducing German official in favor of German private dollar holdings continually since mid-March.

Foreign private dollar holdings, which had declined substantially in March, showed a rise of more than \$500 million in April, on the basis of the weekly tentative data. Even after deducting \$100 million for the intra-German swaps just mentioned, this rise is abnormally large. In the entire year 1963, the increase in foreign private dollar holdings was just \$1 billion, and this figure was higher than for any other recent year.

Taking the first four months of the year as a whole, the deficit, conventionally calculated, would be at a seasonally adjusted rate of about \$1 billion. On the basis of "official settlements," adjusted for the intra-German swaps, the balance would show a substantial surplus. U.S. monetary reserves increased in that period by \$50 million. U.S. gold holdings rose \$130 million and official holdings of foreign convertible currencies \$50 million, while the net U.S. position in the IMF deteriorated by \$130 million, mainly reflecting the U.S. drawing of \$125 million.

Abroad, the most recent period has shown little change. It remains uncertain how far the advice to member countries of the Common Market authorities to give price stability priority over all other policy goals will be followed, and whether the anti-inflationary measures of Italy, France, and the Low Countries will turn out to be adequate, or insufficient, or excessive. Germany, the one member country where inflationary price and wage increases do not seem to pose an immediate problem, has so far done little or nothing to correct its trade surplus, which is now running at an annual rate of nearly \$2-1/2 billion.

Chairman Martin then called for the usual go-around of comments and views on economic conditions and monetary policy beginning with Mr. Treiber, who presented the following statement:

The business situation continues to be characterized by strength and good prospects for further growth. There is no evidence yet, however, that we are entering upon an unsustainable boom. The estimated Gross National Product for

the first quarter of 1964 (\$608.5 billion at an annual rate) is larger than most observers had expected. Final expenditures (GNP excluding inventory investment) showed the largest rise since late 1961. On the other hand, some indicators for March and April were not buoyant. Presumably it is too early for the effects of the recent Federal tax cut to show up in increased retail sales. The most recent estimate of expenditures for plant and equipment shows a good increase but not necessarily of boom proportions.

Recent corporate reports have shown great increases in corporate profits. In many cases there has been merely a return to former ratios of profits to sales and of profits to capital that in the past have been considered reasonable and appropriate to promote further investment. It is good to see increased corporate profits, after more than three years of continuing rising business activity; perhaps the most significant aspect of this performance is the generally good cost control which it reflects. Improved corporate profits will be, undoubtedly, a factor in wage negotiations later in the year.

The broadest price indexes continue to show considerable stability. In the last few weeks there have been few announcements of price increases for individual commodities. Over the last couple of months, the prices of sensitive industrial raw materials have shot up strongly; but during the last week or so they appear to have leveled off.

The interpretation of recent commercial bank credit data is especially difficult because of the problems of seasonal adjustment. There is no clear evidence as yet that the underlying pace of bank credit expansion is significantly different from the 1963 average, which was rather substantial. Senior loan officers at the large New York City banks consider loan demand good but not exuberant. There is some evidence that increased loan demand is felt more in areas outside of New York City. Many business concerns have sufficient resources to enable them to make large expenditures without substantial recourse to the banks.

After recording a good surplus in March, our balance of payments has registered a large deficit in April. To some extent, however, the March surplus and the April deficit reflect movements out of and then into U.S. dollar time deposits in Canadian banks. The large expansion of our exports in recent months has been most welcome, but we cannot count on a continued large increase; indeed, exports could decline in the coming months. Imports rose in March and it

appears likely that there will be a further increase. Long-term bank lending to foreigners continues strong. We can also expect an increase in foreign capital issues in U.S. markets. The confidential, highly tentative estimate made by an intra-Governmental group indicates a balance of payments deficit of \$1.9 billion for 1964. Another deficit this year in such a sizable amount, following a sequence of even larger deficits over the last several years, raises serious questions as to how this year's deficit will be financed. Inflation at home could make the deficit worse.

The domestic economy is continuing to expand without either great pressure in the financial markets or generally rising prices. A variety of developments, such as closer-to-capacity output in some industries, the forthcoming wage negotiations and the continuing ample liquidity of business, could change this situation and lead to inflationary pressures. At least for the moment, however, there appear to be a number of forces serving to restrain these pressures. These forces include lack of speculative excesses in the current expansion, a high level of savings, the settlement of the railway-labor dispute, and the psychological restraint arising from uncertainty about the impact of prospective cutbacks in defense spending.

On the balance of payments side, the disappointing figures for the first weeks of April underline the need to regard the unexpectedly favorable first-quarter results as due in part to special circumstances. It is likely that the balance of payments will continue to be a problem throughout the year, and efforts to improve our international payments position must be pursued relentlessly. Recent declines in U.S. Treasury bill rates have apparently not led to significant adverse short-term capital movements, but this result has been due mainly to simultaneous declines in such foreign short-term rates as the Canadian Treasury bill rate and the Euro-dollar rate. Lower rates in competing financial markets cannot be counted on in the future. Indeed, it is likely that a number of important foreign countries will move toward firmer monetary policies with accompanying rises in interest rates.

"Even-keel" considerations in connection with the current Treasury refunding operation preclude a significant policy change at this time. No change in the directive appears to be called for, except an insertion of the usual reference to the Treasury financing and some rewording of the reference to the balance of payments in order to reflect the most recent

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developments with respect thereto. Specifically, I would suggest that the last sentence of the first paragraph of the present directive be revised to read substantially as follows:

"This policy also takes into account the fact that the sharp improvement in the balance of payments in the first quarter of 1964 reflects some temporary favorable factors and that efforts to achieve a lasting improvement in our international payments position must continue undiminished."

In the absence of the "even-keel" constraint, it would seem desirable to take action to reverse the recent declines in Treasury bill rates. The downward trend in bill rates has been accompanied by some tendency toward an easier tone in the money market generally; I think that the restoration of a somewhat firmer tone in the market would be entirely consistent with the policy objectives of recent months. Hopefully, this would come about through a natural reversal of some of the factors that have tended to produce an easier tone. If it does not, it should be possible, when "even-keel" considerations cease to be a constraint, to move toward the restoration of a firmer tone. By the time of the next meeting of the Committee, it may be that some move toward less ease will commend itself in the light of the balance of payments problem.

Mr. Ellis commented that New England illustrated that a manufacturing region could prosper without growth in manufacturing employment. Factory output was holding about 2-1/2 per cent above year-ago levels, but factory employment, which accounted for 36 per cent of total employment in the District, currently was running 1.7 per cent below a year ago and somewhat below the level of three years ago. The answer, of course, was that the decline in manufacturing employment was offset by rises in other kinds of employment, including government, services, and trade. Construction contract awards in the early part of the year were 21 per cent higher than a year ago, and construction employment was more than 12 per cent

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ahead of last year. Somewhat inconsistently, March construction awards for manufacturing were 6 per cent below year-ago levels although final tabulations of manufacturers' capital outlay intentions in the Reserve Bank survey suggested a 16 per cent gain for the year as a whole.

Commercial banks in the District faced a strong loan demand, Mr. Ellis said. On a seasonally adjusted basis, business loans had increased in each month since last November with the first quarter total showing a gain of 4.4 per cent. Demand deposits in April showed little change from the first quarter level, but time deposits were up considerably, largely because of increases in negotiable certificates of deposit. Asset shifting out of short-term Governments and into municipals had continued to the point where holdings of these Governments by weekly reporting banks outside of Boston were at the lowest point since 1957. Loan-deposit ratios for all banks in the District had reached 70.4 per cent, a postwar record high.

Mr. Ellis said he would like to congratulate the staff on the improvement in the memorandum on economic and financial conditions. He thought it quite accurately documented the statement that economic expansion continued at a moderate pace. However, he would want to deliberate about the proposition that we were witnessing a "balanced" economic growth. With bank credit increasing at an annual rate of 11 per cent, as it had in the past three months, he was unwilling to conclude in advance that the situation was necessarily balanced. He had found helpful the

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appendix note on the duration of business expansions. Of course, this subject was of significance only if one believed the economy was still subject to cycles of boom and recession. If one operated on such a belief, by the thirty-eighth month of expansion it would seem almost as a matter of definition that monetary policy, which had been almost unchanged for nine months in a posture of ease, should be gradually shifted into a position of neutrality to help contain any inflationary pressures that might be developing. During the present Treasury financing, however, it was important to follow an even-keel policy.

With respect to the directive, Mr. Ellis said that he preferred alternative B of the staff drafts for the first paragraph. In a final comment, he suggested that the staff include an appendix in its next economic and financial report discussing the relationship between measures of capacity utilization and the existence of upward price pressures.

Mr. Irons reported that economic activity in the Eleventh District was strong in March, but advancing only moderately. Prospects were that the figures would show further moderate advances in April and May. Industrial production dropped a bit in March due to a decline in petroleum output, but some improvement in April and May seemed probable as a result of increases in manufacturing output. Construction of virtually all types was very strong, and further advances probably occurred in April and were expected in May. The employment situation in the District was satisfactory. Unemployment in March was at a seasonally unadjusted rate of 4.6 per cent. The estimates of employment agencies for April and May were favorable.

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District department store sales were steady at a high level, Mr. Irons continued, and automobile registrations were running ahead of a year ago. Agriculture was mixed; there were generally improved soil conditions as a result of scattered rains, but weaknesses in cattle markets were having an adverse effect.

In the financial area, Mr. Irons said, bank loans were down a bit in all categories except consumer and real estate. Investments were up slightly in total; holdings of Governments were down and non-Governments were up. Demand deposits showed strong growth, but there had been some moderate decline in time and savings deposits.

As he saw the national economic situation, Mr. Irons said, moderate expansion was continuing with no signs of ebullience giving warning of imminent inflationary developments. The situation was pretty well balanced, although he recognized the deterioration of the balance of payments in April. He thought the current Treasury financing called for maintaining the status quo in the money market, and maintaining bank reserves about as in the past three weeks. Such a policy would be desirable, in his opinion, even if the Treasury financing was not in the picture. He would hope that free reserves would be around \$100 million plus or minus \$25 million, and member bank borrowings in the \$150-\$250 million range. He would like the Treasury bill rate to be within a range of about five basis points or so of the discount rate, and the Federal funds rate mostly at the discount rate.

Mr. Irons said he would not change the directive except to include a reference to the Treasury financing and possibly to make some reference to the deterioration of the balance of payments in April. In his judgment the economic situation probably was strong enough to withstand some slight firming without adverse effect if conditions were to move that way, but he also thought there would be no danger in maintaining the status quo for the next three weeks. However, he would lean toward resolving doubts on the side of less rather than more ease.

Mr. Swan commented that in the Twelfth District economic activity seemed to be about keeping pace with that of the country as a whole in March and early April, but he would characterize the advances in both the District and the nation as modest. Total employment in the District in March was up slightly, but the unemployment rate remained unchanged from February. Manufacturing employment declined again in March and was now about 1 per cent below the December figure. The decline was due to continued cutbacks in defense and space-related industries, which were causing some concern. Notwithstanding the decline in the manufacturing sector, the first-quarter gain in total employment just about matched the gain in the rest of the country.

In the lumber industry, Mr. Swan said, there was some indication in April of a leveling off in orders and prices. Perhaps the mild winter weather had led to some borrowing from the usual spring increase. However, production and shipments were still at relatively high levels.

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Producers were encouraged by their success in recovering a significant portion of what they had lost of the Atlantic Coast market to Canadian mills during last year's strike--although Canadian producers continued to be the major suppliers to that market.

During the first three weeks in April, Mr. Swan said, District weekly reporting banks showed an increase in loans which was more than offset by a decline in security holdings--just the reverse of the changes at the national level. Major banks were still net sellers of Federal funds. The recent decline in bill rates had led to some shift from bill holdings to the Federal funds market. In the first quarter as a whole, total loans and investments of weekly reporting banks declined somewhat more than in the first quarter of 1963. An increase in loans was more than offset by a decline in security holdings. The loan increase, however, also was short of the increase a year ago.

Mr. Swan commented that the Treasury financing required an even keel at the moment. In addition, he saw nothing in terms of consumer or business spending or in the rates of increase so far this year in the money supply and bank reserves that would lead to a need for changing the Committee's general policy position. He would favor no change in the period ahead. The present directive, with the addition of a reference to the Treasury financing, seemed appropriate to him.

Mr. Deming commented that fairly complete economic data for March showed that some slowdown in economic activity had taken place in the

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Ninth District. Both personal income and industrial output showed virtually no change from February. This result apparently reflected adverse weather as much as anything. In April, however, the expansion characteristic of the first part of 1964 seemed to have been renewed. Construction activity was strong; employment seemingly rose more than seasonally, and manufacturing employment was expected to continue to rise more than seasonally for the next several months.

In the important farm sector, Mr. Deming said, prospects seemed generally favorable but there were spotty areas with insufficient sub-soil moisture. The livestock picture was not encouraging, with prices showing quite pronounced weakness.

Banking developments in the Ninth District in April were mixed. Loan demand at city banks continued to show the weakness characteristic of this year so far. Bank investments, however, had shown some increase in 1964 in contrast to a usual pattern of decline. Still, total credit at these banks showed a decline for the first four months, similar to the behavior last year but contraseasonal in general. At country banks, both loans and total credit expanded more than usual in April, and the first four months of 1964 showed strength in both loans and investments. Deposit behavior in both types of banks was quite strong in April, more than offsetting the relative weakness seen in the first quarter. Time deposit growth at both city and country banks was very sharp in April.

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The late April opinion survey of the Minneapolis Bank showed a sharp upward swing in optimism about current economic conditions and near-term prospects, although reporters from farm areas were less optimistic than others. For almost the first time in the current upswing the optimism touched on exuberance in the nonfarm areas.

With respect to policy, Mr. Deming favored an even-keeled position. He thought the directive might be left as it was, with the insertion of a clause referring to the Treasury financing. However, he had no particular objection to alternative A of the staff drafts.

Mr. Scanlon said that recent developments in the Seventh District had not altered the favorable outlook reported at previous meetings.

Output based on electric power data had been rising in most major industrial areas in recent months and was well above last year in all centers. Prospects for a further increase in employment, beyond seasonal proportions, appeared good and unemployment compensation claims had been at a low level.

Evidence on retail sales continued mixed, but as yet there had been no sharp upsurge in consumption purchases following the effective date of the tax cut. Savings increases at savings associations had been less than last year in recent months. High withdrawals in March had been associated by savings and loan spokesmen with the need for funds to purchase AT&T stock.

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According to reports of bankers, farm land values continued to increase appreciably in the District despite declines in farm income. Farm income continued to be affected adversely by relatively low cattle prices, and the current prospect was that prices would continue relatively low with marketings during the second quarter expected to exceed the year-earlier level by about 6 per cent.

Mr. Scanlon said there was nothing in District banking statistics to suggest more than ordinary credit demands by businesses and consumers. In fact, the rise in business loans since the end of January was the smallest in the past five years. Nevertheless, outstandings, especially for manufacturing and trade borrowers, remained at high levels compared with a year ago.

Meanwhile, major Chicago banks showed a greatly improved basic position, although this was mainly attributable to the switch of one bank from heavy buying to heavy selling in the Federal funds market. While their loans and investments declined, these banks sold a substantial volume of CDs last month, presumably in anticipation of future needs, or rising rates, or both.

As to policy, Mr. Scanlon thought there should be no change during the next three weeks. If the directive were changed, it should be for the purpose of clarification, to make reference to the Treasury financing and such minor changes in the language dealing with the balance of payments figures as were necessary, and not to change policy at this time. The current discount rate should be continued, in his opinion.

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Mr. Clay reported that weather conditions had shown marked improvement for agriculture this spring in both the Tenth District and nationally. Although temperatures had been cool, causing the growing season to be late, moisture conditions were substantially better than a year earlier in most regions. In the Tenth District, extreme drought conditions had been broken, except for an area including the Oklahoma panhandle, parts of northern New Mexico, southeastern Colorado, and southwestern Kansas. Prospects for irrigation water, which were unusually poor during the winter, were about normal now because of heavy snow in the mountain areas during March and April.

Contacts with a variety of trade associations composed of retailers who deal with farmers and large distributors of farm supplies indicated that sales to farmers were near or above year-earlier levels. However, there was considerable regional variation in such sales. In areas where cattle feeding was important or where drought prevailed, sales tended to be down. On the other hand, in areas where production of such commodities as cash grain, cotton, and sheep predominated, and where weather conditions were favorable, sales tended to be above year-earlier levels. Nationally, farm tractor sales in the early months this year had been higher than in early 1963, but tractor sales had been off in most of the Tenth District. Wholesale farm machinery sales to dealers for the last six months were up about 5 per cent from a year ago nationally; in the Tenth District such sales appeared to have been about in line

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with a year earlier. Sales of fertilizer and petroleum products had been slightly above year-earlier levels and feed concentrate sales had been slightly below.

Mr. Clay commented that many individual farmers were in financial difficulty because of a combination of factors such as the intense price-cost squeeze and the lower level of some farm commodity prices, and to a substantial degree because of inefficient operating farm units. There continued to be substantial hidden unemployment in American agriculture, and merchants heavily dependent upon those farmers for sales were experiencing difficulty.

In view of the Treasury financing now under way, monetary policy should remain essentially unchanged barring some compelling reason for change, Mr. Clay said. There appeared to be no such reason in terms of either the domestic or the international situations. In fact, economic and financial developments did not call for any shift in monetary policy, even apart from Treasury financing.

So far as the economic policy directive was concerned, Mr. Clay thought that either one of the drafts suggested by the staff for the first paragraph could serve satisfactorily, but alternative B appeared preferable to him. The proposed modification of the second paragraph to take into account the Treasury financing was in order. He believed that no change should be made in the Federal Reserve Bank discount rate.

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Mr. Wayne observed that general business activity in the Fifth District continued to improve, apparently following the national pattern fairly closely. Total nonfarm employment and factory man-hours were at record levels. The Richmond Bank's business conditions survey continued to reflect strong optimism, with manufacturers reporting further gains in new orders, backlogs, shipments, employment, and hours worked. Some labor bottlenecks in construction and manufacturing had reportedly continued to develop in parts of the District and might be contributing to upward pressure on wages.

Among Fifth District major industries, furniture was probably in the strongest position. The Southern Furniture Market two weeks ago added considerably to an already large backlog of orders and some producers were scheduling additional overtime to meet the demand. Cigarette production had apparently returned to about the normal seasonal level after sharp drops in January and February. In the textile industry a tug of war was going on between manufacturers and buyers over the extent to which the recent reduction in the cost of cotton would be reflected in the prices of yarn and cloth. So far little of this reduction had been passed on, and no sharp rebound in forward buying had yet occurred. Thus, the textile situation remained quite confused, but mill operators nevertheless expected the lower costs to improve their profits. Recent legislation had helped improve the farm outlook and 1964 income projections, originally set at 5 per cent or more below 1963 levels, were undergoing some upward revision.

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Loan demand was generally strong, Mr. Wayne continued. Major banks in the District had increased their net purchases of Federal funds and the number of smaller banks at the discount window had risen from an average of 5 or 6 to around 18 or 20.

On the national scene, Mr. Wayne said, the buoyant tone in business expectations had apparently generated renewed fears of upward price pressures in some quarters. The statistical facts, however, lent little support to these fears. The economy currently appeared to be moving ahead at about the first quarter pace, and the leading information to date suggested no impending takeoff toward unsustainable levels. Despite widely publicized increases in some materials prices, general price measures remained remarkably stable and no significant supply bottlenecks appeared imminent. Recent data on housing starts, new and unfilled orders, and business investment intentions showed good strength but no evidence of excesses. Similarly, the current behavior of stock prices and the apparently changing pattern of expectations in the long end of the bond market did not support inflationary fears. The restraining effects of sluggish retail sales and a sticky unemployment rate also appeared to point to the conclusion that, over the near-term future at any rate, no more than a moderate pace of expansion was likely.

In the policy field, the Committee had made no overt change for a number of weeks, Mr. Wayne observed. Favorable developments

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in the balance of payments over the past several months and the absence of any unsettling developments in the domestic economy had allowed the Committee to maintain a comparatively easy reserve situation as a background against which the tax cut could work out its effect relatively free of influence from monetary policy. It was clear that so far the tax cut had not generated any significant inflationary pressures. It had added some strength and staying power, particularly in the area of business investment, to the business expansion which had been going on for more than three years, but that was one of the main purposes of the move and one much to be desired. Consequently, it seemed to Mr. Wayne that Committee policy had been fully justified. The awaited signal that some policy change was needed had not come, and he could see none developing at the moment. For that reason and also because the Treasury would be in the market for the next ten days Mr. Wayne saw no need to change the Committee's policy. He would not change the discount rate. With respect to the directive, the draft of the first paragraph prepared three weeks ago--presented now as alternative B--appealed to Mr. Wayne although some small language changes might be appropriate. However, a renewal of the present first paragraph was acceptable to him. A change in the second paragraph to acknowledge the Treasury financing, as suggested in the proposed draft, was in order.

Mr. Mills made the following statement:

In my opinion, the national economy is in no immediate danger of damaging inflationary pressures that would justify a positive policy of Federal Reserve System credit restraint. On the contrary, available statistical evidence calls for a policy that will foster further expansion in commercial bank credit and thereby encourage a reasonable increase in the money supply.

The first paragraph in the outstanding directive to the Manager of the System Open Market Account seemingly declares for a moderately expansionary monetary and credit policy but, as set out in the second paragraph, only if attainable within the context of existing conditions in the money market. In other words, unless an economically constructive credit policy can be conducted within the boundaries of the existing interest rate structure, credit policy motivations are to be sacrificed to interest rate considerations. As it is impossible to enjoy the better of two relatively incompatible policy worlds, the Committee's directive taken at face value is burdened with a credit restriction bias.

Under these circumstances, the Committee must make a policy choice which, in my opinion, opts for the policy spirit declared in the first paragraph of the directive. Adoption of such a policy would require elimination of the interest rate considerations embodied in the second paragraph. To do so would free the operations of the System Open Market Account from the oppressive atmosphere of interest-rate pegging instructions without having embarked the Federal Reserve System on an aggressive and objectionable policy of credit expansion. This is so because as long as the commercial banking system is permitted to operate on a margin of free reserves, credit expansion can follow. Under present conditions, a small margin of free reserves is sufficient to accommodate a reasonable expansion of commercial bank credit along the line of increasing commercial and industrial loans. The major expansion of bank credit over the last year and more was propelled by the availability of a steadily rising volume of time and savings deposits on which reserves of only 4 per cent are required. This credit expansion in the time and savings deposits area of commercial bank deposits has dangerous implications which will retrospectively deserve study to devise means to prevent a future repetition of whatever evils have resulted.

The upshot of these comments is that reserves should continue to be supplied in a volume sufficient to leave a small margin of free reserves on which commercial bank credit can expand safely. Negative free reserves should be studiously avoided because their existence on a continuous basis would evidence a restrictive credit policy compelling a contraction of credit and placing the money supply under downward pressure.

Mr. Mills added that if credit demands rose as anticipated, the kind of policy he had outlined would lead to a firming of interest rates without the Committee's asserting any drastic policy change.

Mr. Robertson commented that he had great sympathy with Mr. Mills' point of view. He then made the following statement:

With the Treasury engaged in a substantial exercise in debt lengthening at this moment, reducing the liquidity of the private economy in the process, this is certainly no time for us to be rocking the boat. Moreover, even if we were outside an "even keel" period, I would favor a policy of "no change." To me our measures show a more or less appropriate rate of monetary expansion on average over recent months. With the tax cut impact proving gradual (to say the least) and the price picture remarkably stable for this stage of economic expansion, I would not want us to tug on the monetary reins. To call for a little tightening now, in anticipation of trouble that might otherwise develop a number of months down the road, is to demonstrate too little faith in the flexibility and speed of influence of monetary policy, and too much faith in our ability to forecast business. In this one instance, I wish I could say "I'm from Missouri" rather than Broken Bow, to signify that before voting to tighten policy to fight an inflation I want to be shown one.

In a further comment, Mr. Robertson said that he thought the second paragraph of the directive should be revised to refer to the Treasury refunding. He did not see a great deal of difference between

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the staff's alternatives A and B for the first paragraph, although B seemed to read a little more smoothly. He would be willing to accept the present first paragraph without change.

Mr. Shepardson noted that the staff reports indicated a desirable continuing moderate expansion. It was encouraging that there had not been more signs of distortions or of inflationary pressures, such as might possibly have occurred. Also, with the Treasury financing activity at present, the Committee obviously was under some constraint with respect to policy. It was still his feeling that the Committee was in no sense in a posture of restraint; the Committee's policy was one of ease, and the degree of ease was a little greater at this point than seemed desirable. He recognized that any immediate change would be inappropriate because of the Treasury financing. However, he hoped there would be no action to offset any lessening of ease that might occur in the market following the financing. He felt as Mr. Ellis did, that there had been a long period of expansion in credit, and that it might be well to ease off in the rate of that expansion as soon as the Treasury situation permitted.

Mr. Mitchell said he favored no change in policy. He did not think a change in the directive was necessary, although he had no objection to small language changes if the Committee felt they were desirable.

Mr. Daane said the Treasury financing clearly called for an even keel policy. He did not subscribe to Mr. Irons' view that the Desk should resolve doubts on the side of less ease in implementing such a policy. With respect to Mr. Irons' proposed free reserve target of \$100 million plus or minus \$25 million, Mr. Daane said he had a strong feeling that such an instruction to the Desk was too restrictive, and that it was unwise to seek so narrow a range of fluctuation. He would like to see a much wider range given as a guide to the Desk, and he would hope that this would represent the consensus of the Committee.

Apart from the Treasury financing, Mr. Daane said, there seemed to be nothing in the domestic economic or credit situation or in international rate relationships that would call for a change in policy. He was puzzled by Mr. Treiber's statement that he would like to see a restoration of a firmer tone in the money market. The review of the New York Bank clearly characterized conditions as generally firm except for comfortable conditions near the end of statement weeks, associated with sharp changes in float or with redistributions of reserves towards the money markets. There was nothing in the supplemental report of the Manager that indicated anything other than a steadily firm money market. Accordingly, he would dissent from the view that the Committee should restore a firmer tone in the money market.

Mr. Daane favored no change in policy and no change in the directive except the addition of a reference to the Treasury refunding.

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Mr. Hickman said that despite a sharp rise in disposable personal income since the tax cut, consumer spending for goods had not yet exhibited any evidence of the progressive stimulus expected in some quarters. In fact, on the basis of incomplete data for April, retail sales had held just about even with March, after adjustment for seasonal variation and the changing date of Easter, or possibly had declined slightly.

Production, on the other hand, had been more buoyant, largely because of strength in steel and autos, with an assist from other durables. In the case of steel, production during the first 25 days of April was at a seasonally-adjusted annual rate of 125 million ingot tons as compared with March's figure of 118 million tons. Fourth District orders were especially strong in April, according to confidential reports, suggesting continued strength in ingot output in May. Auto output in April amounted to about 780 thousand cars domestically produced. That would amount to a seasonally-adjusted annual rate of 8.51 million cars, including output of cars for export. The corresponding March figure was an annual rate of 8.26 million cars. Auto inventories, already at record levels, increased further during April. Industry sources reporting to the Cleveland Bank suggested that no further production strength should be looked for from this industry during the current model year, barring an unexpected surge in sales.

Turning to policy for the next three weeks, Mr. Hickman said that with the Treasury's exchange of securities scheduled for May 15 the Committee's hands were tied for the next ten days. Following customary procedures, the Committee would not want to shift policy significantly between meetings.

In his opinion, Mr. Hickman continued, the tone of the money market had shown continued ease since the last meeting of the Committee, as reflected in the lower yield curve for U.S. Government securities, the rate on Federal funds, and municipal yields. Free reserves during the past three weeks appeared to have been somewhat more closely on target than during the previous three weeks, but reserves had been distributed in favor of the central money markets, which largely accounted for the easier tone.

Thus far this year the money supply narrowly defined had increased at an estimated annual rate of 3.9 per cent. This compared with a 3 per cent increase in the corresponding period a year ago and 2.8 per cent for all of 1963. Money supply plus time deposits had increased at a 7.1 per cent annual rate thus far in 1964, which compared with 8.1 per cent in both the year-ago period and all of 1963. These percentages were based on seasonal adjustments made by the Board staff. Using seasonal factors developed by the St. Louis Bank, the increases this year and in the corresponding period of 1963 were even larger. Thus, recent growth of the money supply had been substantial, no matter how measured.

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Mr. Hickman said he concluded, as he had three weeks ago, that recent policy had been easier than was desirable. The Treasury refunding required an even keel policy, but this should not prevent the Committee from probing towards money market conditions that were consistent with a more modest rate of monetary expansion. He would opt for Mr. Irons' suggestion of a free reserve target of \$100 million plus or minus \$25 million. He recognized, however, that it might be necessary to widen the range if problems were created by a change in the distribution of reserves. With respect to the directive he preferred alternative B of the staff drafts for the first paragraph.

Mr. Bopp reported the economy of the Third District was showing gradual improvement, with unemployment claims lower than for two years. Retail sales remained sluggish relative to those in the nation. Banks in the Third District had been able to cover most of their basic deficiencies in reserves through the Federal funds market.

An even keel policy was called for in the next three weeks to facilitate the Treasury financing currently under way, Mr. Bopp said. Even in the absence of Treasury financing, however, a policy aimed at maintaining prevailing conditions of reserve availability and interest rates seemed to him the most prudent course. Conditions with respect to resource utilization, prices, and balance of payments did not justify a movement toward greater restraint at this time.

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Moreover, Mr. Bopp continued, the strength of future expansion was still an unknown quantity. Symptomatic of this uncertainty was some concern over the lack of visible effects of the tax cut. While this concern might prove to be ill-founded, it seemed sufficient reason for a wait-and-see position.

Mr. Bopp said he would not change the directive, except to include a reference to Treasury financing, nor the discount rate.

Mr. Patterson reported that a general feeling of confidence prevailed among businessmen and bankers in the Sixth District that the current economic expansion will continue. Although the degree of ebullience seemed to exceed performance as measured by the statistics, it had to be admitted that the most recent data provided more support for such a view than did the figures earlier this year.

There was a strong loan demand at the Sixth District leading city banks during April. This April's substantial increase compared with a decline in the corresponding weeks of 1963 and a more modest increase in 1962. Real estate, interbank, security, business, and consumer loans all contributed to the gain.

Sixth District leading city banks were apparently in a stronger cash reserve position to meet the loan demand than banks throughout the country. The April loan increase was accompanied by no decline in U.S. Government security holdings, contrary to the experience of banks elsewhere. District banks also increased their

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holdings of municipalities, although the rise was weaker than in the comparable period of 1963. During the week ended April 22, the banks maintained their reserve positions partly by a substantial net purchase of Federal funds, but purchases about equaled sales on an average during the preceding four-week period. Relatively few banks were borrowing, and total borrowings in April averaged about the same as in March.

The March loan figures, available for all member banks as well as for those in leading cities, showed a seasonally adjusted rate of increase slightly under that for the United States although the rate of increase from a year ago was greater, Mr. Patterson said.

The vigorous loan demand reflected what was apparently a slightly greater rate of economic expansion in the District than in the United States. For example, in March nonfarm employment in the District was 3.2 per cent above that of a year earlier compared with an increase of 2.7 per cent for the nation. The seasonally adjusted month-to-month increases this year had exceeded the national gains. Insured unemployment at 3.3 per cent had been reduced to the lowest level since 1953.

Employment in most manufacturing categories was up in March, Mr. Patterson said, with the strongest increases in primary and fabricated metals and in transportation equipment. An unauthorized walk-out at the Atlanta General Motors plant of 275 chassis workers

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that threatened to idle 3,150 workers was settled last week. Most of the increase in nonfarm employment had come outside the manufacturing area, however, with improvement in construction being the most pronounced.

Prospects for increased employment were implied by recent announcements in connection with the NASA Apollo manned lunar landing program activities. These activities directly affected four of the six District States: in Florida at Cape Canaveral (or Cape Kennedy) where the rockets were launched; Michigan at New Orleans where the Saturn I, Saturn IB, and Saturn V first stages were being manufactured; in Mississippi where ground test operation facilities were being constructed on the Pearl River in Hancock County (west of Gulfport), and in Alabama at Huntsville where the Marshall Space Flight Center was located. The Federal budget proposal for fiscal 1965 included construction expenditures of \$61.9 million at the Mississippi test center, \$15.2 million at Huntsville, and \$6.5 at New Orleans. Large expenditures had, of course, already been made and were being made at all these operations. Last week IBM announced that it would add 800 employees to its operations in Huntsville where it was developing the instrument units.

On the other hand, Mr. Patterson said, the net impact of cutbacks in defense installations and the reduction in the production of nuclear materials had been minor. No closings of major defense

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installations had been announced for the District. The cutback in the United States production of enriched uranium at Oak Ridge, Tennessee, was expected to reduce employment by only 125. The principal effect will be a 445,000 kwh reduction in the consumption of TVA electricity. Growing demands elsewhere would more than absorb the output released.

Textile executives were expecting some pick-up in demand, at least in the short run, to develop from the recent cotton legislation. They believed that buyers who had been holding off would enter the market as soon as the price situation was clarified. On the other hand, there were rumors of a forthcoming wage increase, partly reflecting the difficulty the industry was experiencing in retaining a work force because of competition from other types of manufacturing.

There were less rosy reports, of course. Consumer spending, although high, had not increased as much as some persons had hoped it would in response to the tax cut. There were metropolitan areas where residential construction activity was apparently lower than last year, although contracts for the first three months this year exceeded those of the corresponding period last year in 21 of the 26 metropolitan areas. In Atlanta and Birmingham, mortgage bankers were concerned about the possibility of excessive commercial and apartment building. At the same time they were talking about the possibility that the cost of mortgage money would increase, basing

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their forecast upon the reduced inflow of funds at savings and loan associations and the narrow spread between current yields on Government securities and mortgages. In general, however, such worries were well submerged by a feeling of optimism.

Mr. Shuford said that in the St. Louis District the indicators were mixed but there appeared to have been some hesitation since January in the upswing of business activity. Employment and industrial use of electric power in the major metropolitan areas had changed only slightly since January. Spending, as measured by bank debits and department store sales, had declined somewhat. Business loans at weekly reporting banks had regained a major portion of the decline of late last fall. Bank deposits had continued to rise at a rapid rate.

As had been indicated around the table, Mr. Shuford said, in view of the current Treasury refunding it was clear that the Committee should follow a policy of even keel. However, he would not be disappointed if after the even keel period the bill rate moved back to 3.50 per cent. Free reserves might average somewhere around the \$100 million level, and there might be a somewhat reduced rate of expansion in the money supply. As Mr. Hickman had indicated, using the St. Louis Bank's seasonal adjustment factors, the money supply had been rising at an annual rate of 5-1/2 per cent since the first of the year.

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Mr. Shuford said he thought that the first paragraph of the current directive would be satisfactory, perhaps with a small change in the sentence relating to the balance of payments. He also found alternatives A and B acceptable, and he approved of the staff draft for the second paragraph.

Mr. Baiderston said it was clear that the Treasury financing took precedence between this and the next meeting. He would note only that the level of member bank borrowings in April did not seem to indicate as much restraint as the Committee might have thought was being applied. As to the directive, he preferred alternative B with the language changes suggested.

Chairman Martin said he had little to add to the discussion. He liked alternative B of the staff drafts, although he had no objection to some changes in its language. He had concluded from the comments around the table that alternative B also was preferred by a number of others.

After further discussion, Chairman Martin suggested that the Committee vote on a directive the first paragraph of which would consist of alternative B as originally drafted, and the second paragraph of which would include a reference to the current Treasury refunding but would be unchanged otherwise.

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Thereupon, upon motion duly made and seconded, and by unanimous vote, the Federal Reserve Bank of New York was authorized and directed, until otherwise directed by the Committee, to execute transactions in the System Account in accordance with the following current economic policy directive:

It is the Federal Open Market Committee's current policy to accommodate moderate growth in the reserve base, bank credit, and the money supply for the purpose of facilitating continued expansion of the economy, while fostering further improvement in the capital account of U.S. international payments, and seeking to avoid the emergence of inflationary pressures. This policy takes into account the expected stimulus to domestic activity from the recent Federal income tax reduction, and the increases projected for the year in business capital expenditures. It also gives consideration to the continued relative stability in average commodity prices; the country's improved, though still difficult, international payments position; and the interest rate advances over past months in important markets abroad.

To implement this policy, and taking the current Treasury refunding into account, System open market operations shall be conducted with a view to maintaining about the same conditions in the money market as have prevailed in recent weeks, while accommodating moderate expansion in aggregate bank reserves.

Chairman Martin then noted that copies had been distributed to the Committee of a letter dated April 22, 1964, from the Honorable Wright Patman, Chairman of the House Banking and Currency Committee and of its Subcommittee on Domestic Finance, discussing further the question of making available to the Subcommittee the Federal Open Market Committee's minutes for the years 1961-1963.

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Copies also had been distributed of a proposed reply, reaffirming the position taken by the Committee at its meeting of April 14, 1964, that it would not be in the public interest to make the minutes for years subsequent to 1960 available to the Subcommittee at this time. Chairman Martin indicated that he would have to leave the present meeting shortly and he would appreciate having an expression of views with regard to the position in the proposed reply, as distinct from the language employed.

Mr. Mills indicated that he was inclined to reverse the position the Committee had taken at the April 14 meeting, in light of Mr. Patman's statement that the Subcommittee would cooperate fully in deleting from the minutes references to materials that should not be made public. He doubted that the Open Market Committee should imply that a committee of Congress was not suited to see its minutes because of their confidentiality. He also was concerned about certain statements in the draft letter.

Mr. Robertson said that he, too, was inclined to reverse the Committee's earlier position. He did not see how the request could be denied if sensitive material was to be deleted before the minutes were made public. He doubted that the public interest would be injured by turning over minutes five months after the fact; the only possible injury would be to the Committee itself, by reducing the freedom of discussion at meetings. He did not think this alone was sufficient grounds for refusing to comply with the request.

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Mr. Mitchell commented that it was not clear to him from Mr. Patman's letter what the Subcommittee's intent was with respect to who would decide on necessary deletions. If the Subcommittee intended to reserve the right to make such decisions, he would agree with the position taken in the proposed reply.

Mr. Balderston commented that this question had been covered in the course of the hearings, and he had no doubt that the Subcommittee intended to make such decisions itself. Mr. Daane concurred in this view.

Chairman Martin said that an effort to delete sensitive material would require a line-by-line study of the minutes, and he did not think that this was feasible. In his view it would be a mistake for the Committee to modify the position it had taken on the matter at its April 14 meeting. Messrs. Treiber, Balderston, Daane, Shepardson, Hickman, and Wayne expressed agreement.

Chairman Martin then withdrew from the meeting. Upon motion duly made and seconded, and by unanimous vote, Mr. Balderston was elected to serve as Acting Chairman for the remainder of the meeting.

Thereupon, Mr. Balderston called for a vote on the question of whether the position taken at the April 14 meeting with respect to the request of the Domestic Finance Subcommittee for Committee's 1961-63 minutes should be reaffirmed. It was unanimously agreed that Chairman Martin should be recorded in favor of reaffirming this position, in view of his statement before leaving the meeting.

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Votes in favor of reaffirming the position taken previously: Messrs. Martin, Balderston, Daane, Pickman, Mitchell, Shepardson, Shuford, Swan, Wayne, and Treiber. Votes against reaffirming this position: Messrs. Mills and Robertson.

Messrs. Bopp, Clay, Deming, Ellis, Irons, and Scanlon indicated that they would have voted in favor of reaffirming the previous position if they had been members of the Committee at the present time.

It was agreed that any suggestions for revisions of the language of the proposed reply to Mr. Patman should be transmitted to the Secretary, and that decisions with respect to the specific language of the reply would be left to the judgment of Chairman Martin.

Secretary's Note: Under date of May 6, 1964, the following letter was sent to the Honorable Wright Patman, Chairman of the Banking and Currency Committee, House of Representatives, over the signature of Chairman Martin:

After carefully considering your letter of April 22, 1964, reiterating your request for the 1961-1963 minutes of the Federal Open Market Committee, the Committee has reaffirmed its decision as reported to you in my letter of April 14.

Your letter expresses your disappointment with this decision, but we feel this may arise from a misunderstanding of the situation. You describe our decision about the minutes as "a refusal to allow the Members of the House whose duty it is to oversee the administration of the Nation's money, information vital for determining whether the Federal Reserve is carrying out the mandate of the Federal Reserve and Full Employment Acts." If this were the case, you would have every right to be not only

disappointed but deeply disturbed. But let me try to show you why it is not the case.

The Federal Reserve System has cooperated fully with your Subcommittee, and will continue to do so. The members of the Board of Governors, the Presidents of the Federal Reserve Banks, and the staffs of the Board and the Banks have given freely of their time to discuss our operations with members of your Subcommittee and your staff. Your staff has been given every item of information they have asked for about System operations, ever including the handwritten notes in the worktrunks that the Board's examiners use in examining the Reserve Banks. Thousands of man-hours have been devoted to answering questions submitted by you and your staff regarding the Federal Reserve and the commercial banking system. Where we have not had the information, the staffs of the Board and the Banks have worked assiduously to develop it. In some cases where your inquiries ran beyond our immediate internal operations, the Board has arranged and paid for outside contractors to help in developing and processing the data requested. We have thus demonstrated our desire to respond fully to your requests for information, and you have publicly acknowledged our cooperation.

You have often ascribed great power to the Federal Open Market Committee, greater power than I think we have. But we both agree that the Committee has an important job to do. The other members of the Committee and I are convinced we can do a better job if we are allowed some privacy when we meet together to discuss how best to perform the functions the Congress has assigned to us. Congress and the public are entitled to know what actions are taken as a result of these discussions and the reasons for these actions, and we make this information public in a variety of ways, as you know. But, for the reasons previously explained to you, we think our most recent minutes should not be published. These reasons were set forth in my letter of April 14, copy attached, and in a letter of September 11, 1962, to you as Chairman of the Joint Economic Committee, the pertinent portion of which is also attached.

If the System's performance cannot be evaluated on the basis of information already supplied, it is difficult to understand what will be derived from the minutes to aid in this endeavor. You have publicly described the minutes as written in an "unknown language" and expressed doubt that you would get any information from them if you had them.

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You have said that when you had the 1960 minutes you "had to ask the staff to explain them, and the staff could not explain them, so we got two of the best experts in the United States, and they were going to interpret them for us and tell us what they meant" but unfortunately it "took them nearly a year." (Hearings, "The Federal Reserve System After Fifty Years," Vol. 1, p. 737.) Let us suggest that there is an easier and more effective way: tell us what you are looking for, and we will see if we cannot get you the answers more quickly than that.

We recognize that there may be interest in the procedures of the Federal Open Market Committee, that is, in the conduct of the Committee's meetings and the nature of discussions that take place in them, and for that reason we are making the minutes available to interested persons for years prior to 1961 by depositing them in the National Archives. This will serve the needs of both the Congress and students of monetary policy, without running the risk of disclosing matters sufficiently current to be damaging to the public interest.

We think that this risk is real, despite your assurance of cooperation in minimizing it. The difficulty of avoiding inadvertent disclosures is a fact of life, casting no reflection on any individual. On the one occasion when we furnished minutes to a Committee of Congress, the "translation" of them, containing lengthy quotations from them, found its way into the hands of the press. These things happen, and we think it best not to take the chance of their happening again, when we are ready to supply whatever information you seek without running this risk.

Before this meeting there had been distributed to the members of the Committee a report from the Special Manager of the System Open Market Account on foreign exchange market conditions and on Open Market Account and Treasury operations in foreign currencies for the period April 14 through April 29, 1964, and a supplementary report covering the period April 30 through May 4, 1964. Copies of these reports have been placed in the files of the Committee.

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Supplementing the written reports, Mr. Coombs said he expected no change in the gold stock this week for the twelfth week in a row. The Stabilization Fund now held \$283 million in gold. The Austrians probably would not take any gold this month but the French might be in for their usual 30 tons. They had been taking 30 tons every month for a year or more.

On the exchange markets the most striking--and disappointing--development had been the contraseasonal strengthening of the Swiss franc to its ceiling, at which level the Swiss National Bank had been forced to take in somewhat more than \$40 million. The main reasons for this influx of dollars into Switzerland seemed to have been some backwash of funds from Germany following the withholding tax proposal by the German Government and, more importantly, a further tightening of credit conditions in Switzerland. Swiss National Bank officials continued to suggest that the tightness of credit was attributable to temporary factors. Mr. Coombs had the impression, however, that the problem was more deep-seated and might remain troublesome for some time to come. Furthermore, the Swiss would be moving into their period of seasonal surplus within a few weeks' time and this might accentuate still further the buying pressure on the Swiss franc.

Meanwhile, Mr. Coombs said, the Account had lost ground in its efforts to liquidate the outstanding drawings of Swiss francs, having been forced to make a \$25 million drawing on the Swiss National Bank

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to absorb part of its surplus dollar holdings, and it might have to make another \$25 million drawing on the Bank for International Settlements within the next week or so to clean up the remaining dollar surplus on the books of the Swiss National Bank. Such a second drawing of \$25 million would increase the U.S. Swiss franc debt to \$225 million as compared with the total Swiss franc credit lines of \$300 million.

Mr. Coombs said he hoped that at the Basle meeting this coming week end arrangements would be completed for a swap deal between the Swiss and Italians which would provide the Bank of Italy with possibly as much as \$100 million of Swiss francs. He was hopeful that the Bank of Italy would sell these Swiss francs to the System against dollars, which would enable the Account to cut its Swiss franc debt by \$100 million, while the Bank of Italy would simultaneously use the dollars to clean up the remaining \$100 million of its swap drawing upon the System. This, he thought, would be a useful and logical operation.

Even if this deal should go through, however, the Account would be left with a Swiss franc debt of \$100-\$125 million equivalent, with time rapidly running out before the Swiss moved into their seasonal surplus during the summer months. The Fund and Bank meetings in September, the British election in October, and the U.S. election in November might well result in further buying pressure on the Swiss franc. There was some risk, therefore, that serious delays might be

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encountered in liquidating the Swiss franc debt through open market purchases of Swiss francs.

In view of this prospect, Mr. Coombs thought it was prudent to assume that special operations might be required to pay off the Swiss franc debt. As far as he could see, there were two main alternatives: first, that the Account simply buy Swiss francs with dollars, which would probably force the Swiss National Bank to convert such dollars into gold; or, secondly, that an effort be made to negotiate the placement, with either the Swiss National Bank or the Swiss Confederation, of a Swiss franc bond issued by the U.S. Treasury. He was inclined to favor the second alternative. If, however, this was not acceptable to the Swiss and they chose to take gold, there would be some advantage in the fact that the transaction would reconfirm the willingness of the United States to honor these obligations in gold if necessary. He would be exploring the problem with both the Treasury and the Swiss and would hope to be able to report to the Committee more fully at the next meeting.

Mr. Hickman commented that announcement of a large gold sale might possibly produce an adverse public reaction. Mr. Coombs responded that he would hope that a gold sale could be avoided, and that the Swiss would be willing to accept Treasury bonds. The problem had been produced by the Swiss policies, and it was reasonable to expect them to cooperate in meeting it. On the other hand, foreign central

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banks were willing to hold dollars because of the belief that they were freely convertible into gold. If this belief was undermined, the situation would be serious.

Mr. Treiber commented that it was highly desirable for the System to reduce its Swiss franc debt now, to leave room for meeting problems in the coming period of uncertainty. Mr. Coombs expressed agreement, and added that in the long run the U.S. might save rather than lose gold by reducing its debtor position now.

Thereupon, upon motion duly made and seconded, and by unanimous vote, the System Open Market Account transactions in foreign currencies during the period April 14 through May 4, 1964, were approved, ratified, and confirmed.

Mr. Coombs said he wanted to report to the Committee on a matter involving the way in which the Account reported to foreign central banks on the swap operations. As authorized by the Committee, he had been informally reporting the System's current swap position to foreign central bank officials. On the occasion of a System drawing, he would advise the other central bank involved orally with respect to all of the System's drawings, on a country-by-country basis, so that they would be fully informed on the System's debtor position. The System's creditor position with respect to individual countries was reported only with the approval of the country involved; otherwise, only the System's aggregate creditor position was given. He presumed that this information usually was passed on in the same informal way to Government officials, with appropriate safeguards. The arrangement was reciprocal.

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This informal reporting arrangement, Mr. Coombs said, had important advantages in terms of security. An example of the risks involved in more formal interchanges was provided by the experience of the Gold Pool. For a number of months it had been the practice to prepare confidential multilithed reports detailing the Pool's operations. Through one channel or another these reports were regularly leaked to the press, and this was acutely embarrassing to all concerned. The basic problem was that a reproduced document could be handed on with little possibility of detection. Informal oral transmission of information afforded much better guarantees that security would be safeguarded, since no recipient of information could be certain that anyone else had received information in identical form. There had been no leakage of information to the press since an oral reporting arrangement was adopted by the Gold Pool.

For a year or so, Mr. Coombs continued, certain countries had been urging that a more formal reporting system be instituted in connection with swaps, involving a monthly report on all operations to the BIS or some other agency for transmission to governments. The object could hardly be to obtain information, since this already was being provided under the informal system now in effect. He thought the real purpose was to provide a basis for group intervention in the credit operations of individual countries whose positions might be considered overextended at meetings of Working Party 3 or other groups.

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Mr. Coombs said he wanted to alert the Committee to this development. He noted that the subject of formal reporting on swap operations might be put on the agenda at a meeting of the Group of Ten.

Mr. Daane added that the question of formal reports, presumably including information on swaps, to the BIS or some other agency had been referred to in recent Group of Ten Deputies meetings, and it was contemplated that a task force would be asked to consider what data might be requested, on what time schedule, and with what restrictions. Of course, there could be no commitments for the System made in Group of Ten Deputies meetings; the U. S. representatives had stressed that any reporting arrangements would have to be agreed to by all parties, and that there would have to be full reciprocity. The question of what use would be proposed for the data remained open. His own preference was against going too far on formal reporting. He thought it was good that Mr. Coombs had alerted the Committee to take a look at the question, and he noted that it might be necessary for the Committee to formulate a position on the matter at a later date.

Mr. Coombs said he had one recommendation to make to the Committee. The standby swap arrangement with the Bank of England in the amount of \$500 million would mature on May 29, and he recommended its renewal for another one-year period. He had indications that the Bank of England would concur in such a renewal.

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Thereupon, renewal for a further period of one year of the \$500 million standby swap arrangement with the Bank of England, as recommended by Mr. Coombs, was approved unanimously.

The Committee then turned to the proposal of the Federal Reserve Bank of New York to publish the report of the Account Manager to the Committee, which had been discussed without final resolution at the two preceding meetings. Mr. Treiber again reviewed the advantages that the New York Bank saw in publishing this report in the Federal Reserve Bulletin and making reprints available to students and others.

In the discussion, certain problems of publication were noted, including that of partial duplication of other material in the Board's Annual Report and that of differences in tone and emphasis between the Board's and the Manager's reports. It also was suggested that in view of the delay in resolving the question it might now be considered almost moot, particularly since the usual publication delay meant that the report could appear in the June Bulletin at the earliest. Mr. Treiber then suggested that the matter be dropped, and no objection was made.

Mr. Balderston then noted that Mr. Stone had sent a memorandum to the Committee under date of April 27, 1964, regarding the request from the Honorable Wright Patman dated April 6, 1964, for certain information relating to Federal Reserve open market transactions in

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recent years for use in connection with an inquiry by the Domestic Finance Subcommittee of the House Banking and Currency Committee.

(A copy of this memorandum has been placed in the files of the Committee.) Mr. Balderston invited Mr. Stone to comment.

Mr. Stone said that the study in question would actually be made by Mr. George Benston, a staff member of the Subcommittee and a faculty member at the University of Chicago. His discussions with Mr. Benston had been most amicable and satisfactory, and he saw no problems from the viewpoint of the Desk in complying with the request. References to individual dealers would be deleted from the material supplied to preserve confidentiality.

Mr. Stone added that he should mention that the summary tabulations Mr. Benston had requested would be supplied in the form of appendix pages from the Account Management's weekly report to the Committee. These pages contained information not only on transactions in Treasury bills, which was the object of Mr. Benston's interest, but in some cases also on transactions in coupon issues. There were virtually no transactions in coupon issues recorded on the sheets on which bill transactions were recorded during the years for which the data were requested, except for some in 1951 and 1952.

Mr. Mitchell commented that he thought it desirable to provide exactly what had been asked for. Mr. Daane concurred in this view.

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Mr. Balderston asked whether there was any objection to authorizing Mr. Stone to provide the information requested by the Subcommittee on Domestic Finance to Mr. Benston, and no objection was raised.

Secretary's Note: In accordance with this decision, the following letter was sent to Chairman Patman over the signature of Chairman Martin later in the day:

This is in reply to your letter of April 6, 1964, requesting certain information relating to Federal Reserve open market transactions in recent years for use in connection with an inquiry by the Domestic Finance Subcommittee into the operations of the Government securities market. The Federal Open Market Committee considered your request at its meeting today, and is glad to cooperate in providing the information required for this inquiry.

As you may know, Mr. Benston of your staff and Mr. Stone, Manager of the System Open Market Account, have engaged in personal discussions and correspondence in order to arrive at more complete specifications of the materials required and the manner in which they are to be used. Mr. Stone will communicate shortly with Mr. Benston concerning arrangements for physical transmission of the materials in question.

Mr. Balderston noted that a memorandum from Messrs. Sherman and Young had been distributed under date of May 1, 1964, regarding the procedure for making historical minute records of Open Market policy discussions available for scholarly research, and he asked Mr. Young to comment.

Mr. Young summarized the contents of the memorandum, a copy of which has been placed in the files of the Committee. He noted that the National Archives would be prepared to receive the Open Market

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Committee minute records for the period prior to 1961 and to make copies of the material available to scholars and others on a reimbursable cost basis. The Committee earlier had discussed making its records available for the period 1950-60, but it seemed logical that the Committee's entire minute record through 1960, and those of predecessor groups in the System, be made available at the same time, and he and Mr. Sherman so recommended. No restrictions would be imposed on the use of these records other than those customary for appropriate preservation by the National Archives. The main interest probably would be on the part of scholars, although journalists and others might also consult the records.

Mr. Young said the Secretariat had been in touch with the various learned societies, including the American Economic Association, the Economic History Association, and the American Historical Association. All had expressed willingness to cooperate in promoting research based on these records. The Secretariat also had been in touch with the Social Science Research Council. The Council was prepared to set up a committee to suggest types of useful research and to elicit interest on the part of younger scholars.

Upon motion duly made and seconded, and by unanimous vote, the procedures outlined in the memorandum from Messrs. Sherman and Young were approved.

Mr. Balderston noted that it had been agreed at the preceding meeting to hold an afternoon session at this meeting devoted to the

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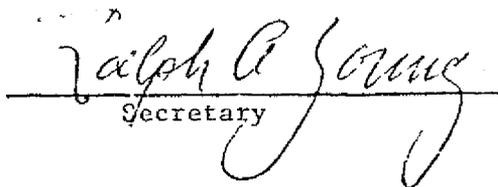
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form and content of the Committee's current economic policy directive. Mr. Ellis observed that he thought such a discussion would be highly desirable. He noted, however, that the staff memorandum on this subject, dated April 8, 1964, did not propose a particular framework for discussion. In his judgment, the discussion would be more fruitful if the Committee had before it an agenda, with specific proposals. He therefore proposed that the discussion be postponed until a later meeting, by which time such an agenda could be prepared.

It was agreed that Messrs. Mitchell, Ellis, and Swan would undertake to prepare an outline for a discussion of the Committee's current economic policy directive at a later meeting. Also, it was suggested that members and other Reserve Bank Presidents forward any proposals they would like to advance to one of these individuals.

It was agreed that the next meeting of the Open Market Committee would be held on Tuesday, May 26, 1964, at 9:30 a.m.

Thereupon the meeting adjourned.


Secretary