A meeting of the executive committee of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System on Tuesday, August 25, 1953, at 10:30 a.m.

PRESENT: Mr. Sproul, Vice Chairman
Mr. Mills
Mr. Fulton, Alternate for Mr. Erickson
Mr. Robertson, Alternate for Chairman Martin
Mr. Vardaman, Alternate for Mr. Evans

Mr. Riefler, Secretary
Mr. Vest, General Counsel
Mr. Young, Associate Economist
Mr. Rouse, Manager, System Open Market Account
Mr. Carpenter, Secretary, Board of Governors
Mr. Sherman, Assistant Secretary, Board of Governors
Mr. Youngdahl, Assistant Director, Division of Research and Statistics, Board of Governors
Mr. Leach, Chief, Government Finance Section, Division of Research and Statistics, Board of Governors
Mr. Gaines, Securities Department, Federal Reserve Bank of New York
Mr. Leonard, Director, Division of Bank Operations, Board of Governors

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the executive committee of the Federal Open Market Committee held on August 4, 1953 were approved.

Before this meeting there had been sent to the members of the committee a report prepared at the Federal Reserve Bank of New York covering operations in the System Open Market Account from August 4 to August 21, 1953, inclusive, and at this meeting Mr. Rouse presented a supplementary report covering commitments on August 24, 1953. Copies of both reports have been placed in the files of the Federal Open Market Committee.

In commenting on developments since the last meeting of the executive committee, Mr. Rouse stated that while the reserve position of banks had been reasonably comfortable during the period, there had developed a feeling of "tightness" in the market which was partly psychological and seemed based to some degree on the view that the Federal Reserve was out of the market. Mr. Rouse went on to say that in view of the position of the executive committee that operations should be such as to keep the market about where it was at the last meeting but, if error were to be made, to make it on the side of ease, he had made repurchase agreements rather freely available and, in the statement week ending August 19, 1953, he had made outright purchases for the System account totaling $25 million. These were regarded by the market to be an indication that the System was prepared to furnish reserves if tightness developed.

Mr. Robertson stated that while he would approve the particular purchases of securities made for the System account, he wondered whether it was desirable for the System account to make "token" purchases of securities unless there was a clear-cut need for more reserves in the market. He suggested that, as a general rule, token purchases might cause uncertainties in the market and generate "guessing" as to credit policy.

Mr. Rouse responded by saying that he felt the specific purchases that had been made had helped to "answer the guessing" that was going on in the market, that he did not think they stimulated any increase in uncertainties, and that they had effectively improved the psychological feeling in the market. The word "token" he thought was perhaps a misnomer and the making of similar purchases at other times, he felt, would depend upon the particular circumstances.

> Thereupon, upon motion duly made and seconded, and by unanimous vote, the transactions in the System Open Market Account for the period August 4 to August 24, 1953, inclusive, were approved, ratified, and confirmed.

Mr. Rouse stated that in view of the prospect that the Treasury might issue special short-term certificates of indebtedness to the Federal Reserve Banks to cover overdrafts in its account at a time when it was approaching the $275 billion statutory limit on the public debt, Counsel for the committee and for the Federal Reserve Bank of New York had been considering whether such certificates came within the $275 billion statutory debt limitation. Mr. Rouse went on to say that he felt certain that such securities would be included, and Mr. Vest expressed the same view.

There was a further discussion of this question and of the possibility that the Treasury might issue special certificates to cover overdrafts that developed inadvertently in such volume as to result in outstanding Treasury obligations temporarily exceeding the $275 billion debt limitation. There was a discussion of the question whether the Federal Reserve Banks should acquire special certificates issued under such circumstances, or whether it would be preferable to show an overdraft in the Treasurer's account at the Federal Reserve Banks. During the discussion, it was suggested that Mr. Vest and Counsel for the Federal Reserve Bank of New York each consider the subject and prepare memoranda for consideration at the next meeting of the Federal Open Market Committee. This suggestion was approved with the understanding that Mr. Vest should feel free to discuss informally with Treasury representatives any questions which he might care to take up with them in connection with the subject, it being understood that the Treasury was also looking into the matter.

Before this meeting there had been distributed a memorandum from Mr. Riefler dated August 21, 1953 to which was attached a draft of proposed letter to the Presidents of all Federal Reserve Banks to inform them that the new procedure for allocating securities in the System Open Market Account on the basis of total assets would become effective September 1, 1953.

Mr. Sproul stated that the Federal Open Market Committee had approved the allocation of securities in the open market account on the basis of total assets of the several Federal Reserve Banks at its meeting on June 11, 1953, that he understood the detailed procedures for such allocations had been approved by the executive committee at its meeting on August 4, 1953, and that if the executive committee approved the proposed letter it would confirm the decision to make the new procedure effective September 1, 1953.

Mr. Leonard called attention to the understanding at the meeting on August 4 that a public statement would be made in connection with the reallocation of securities. Such a statement might take the form of a brief notation on the weekly statement of condition to be issued by the Board as of September 2, Mr. Leonard said, or an alternative would be a somewhat more explanatory statement similar to that contained in Mr. Riefler's memorandum of August 21, which could be included as a note on a separate sheet to be issued with the Board's weekly statement of condition for September 2.

Mr. Mills suggested that the committee approve sending a letter to the Presidents of all Federal Reserve Banks along the lines of the proposed draft with the understanding that the public statement would be similar to that in Mr. Riefler's memorandum and that it would be issued as a part of the September 2 statement of condition.

Thereupon, a letter to the Presidents of all Federal Reserve Banks was approved unanimously in the following form:

"The Federal Open Market Committee, at its meeting on June 11, 1953, approved the allocation of securities in the open market account on the basis of total assets of the several Federal Reserve Banks and directed that detailed procedures for such allocation be prepared. Recommendations with respect to such procedures were made in a memorandum dated July 14, 1953 from Messrs. Rouse and Leonard, a copy of which was forwarded with my letter of the same date. The replies to that letter showed no objection to putting the procedures into effect September 1, 1953 and favored paragraph 7 of the memorandum rather than the alternative paragraph 7.

"Accordingly, with the approval of the executive committee of the Federal Open Market Committee given at its meeting August 4, and reaffirmed at its meeting on August 25, 1953, the procedures set forth in the memorandum dated July 14, 1953 from Messrs. Rouse and Leonard will become effective September 1, 1953 and the reallocation will be made as of that date.

"For your information, enclosed is a table showing the percentages of participation which will be used in the reallocation. These percentages are based on daily averages of total assets of each Federal Reserve Bank for the year ended July 31, 1953. The memorandum also shows what the effect would have been if the securities in the account on August 19, 1953 had been reallocated on the new basis. The usual statement of the actual reallocation will be forwarded to you by Mr. Rouse.

"In view of the relatively large shifts in holdings and changes in reserve ratios which will result in some cases from the reallocation, the executive committee favored issuing a brief statement "regarding the reallocation. This will be done by including the following note in the weekly statement of condition of the Federal Reserve Banks to be issued by the Board as of September 2. The note will appear as an insert between the third and fourth sheets of the statement:

"The statements of condition of the Federal Reserve Banks reflect a reallocation effective September 1, 1953 of securities held in the System Open Market Account. Under the reallocation, participations in the account are based on the size of the Federal Reserve Bank as measured by average total assets. Previously, securities were allocated primarily on the basis of expenses and dividend requirements of the Federal Reserve Banks.

"Settlement for shifts in participations in the open market account between the Federal Reserve Banks is made through the Interdistrict Settlement (Gold Certificate) Fund. The reallocation, therefore, resulted in some changes in reserve ratios of individual Reserve Banks. It did not, of course, affect the reserve ratio of the twelve Reserve Banks combined or the total amount of assets of any Federal Reserve Bank.

"A Federal Reserve Bank should, of course, feel free to amplify the statement in any way considered appropriate."

Mr. Leonard withdrew from the meeting at this point.

Mr. Mills then made a statement with respect to open market policy substantially as follows:

It is proposed that the emphasis on open market policy should be changed from concentration on the status of the Government securities market to concentration on the status of the general economy. Implicit in such a proposal is that open market policy should lead rather than wait on economic events, which contemplates that the near direction of policy should be weighed on the side of relative ease. Implementation of such a policy contemplates that bank credit would be allowed to build around adequate reserves rather than allowing a situation under which action is taken toward supplying new reserves only after their inadequacy is unmistakenly evident. As indicated, an open market policy of this character envisages a relatively easy money market situation. However, should an easier money market fostered by open market policy prove to be conducive to an unwise expansion of bank credit, counteracting measures can be readily employed without harsh results by the following means:

1. Retarding open market action to offset the prospective fall increase in currency circulation.
2. Pinching back the amount of additional reserves that it is expected must be supplied in support of the Treasury's new money financing in mid-fall.
3. Allowing bills held in the System Open Market Account to run off at maturity.

As an open market policy pointed toward greater ease must be carried out through the Government securities market, its status deserves first attention. In that regard the evident intention of banks to retain their recent investments in Treasury tax anticipation certificates is significant for contrary to expectations, where bank liquidation of Government securities has been undertaken it has been via the sale of Treasury bills and not of Treasury tax anticipation certificates. The reserve status of country banks is conducive to their retention of Treasury tax anticipation certificates as they are well supplied with reserves and should not be under early pressure to divest themselves of their holdings of tax anticipation certificates in order to provide themselves with the reserves on which to build their seasonal loan expansion. This is not true of reserve city and central reserve city banks who, having delayed the sale of their tax anticipation certificates, may find themselves under concerted pressure to do so when faced with deposit withdrawals by country correspondents simultaneously with their own seasonal demand for loans. As a consequence, the market could be confronted with heavy selling of tax anticipation certificates which, to the extent that it brought about market weakness, could handicap the Treasury's approaching refunding of its maturing 2 per cent bonds of September 15, 1953.

An open market policy calculated to prevent a situation of this type and at the same time to accomplish the purpose of giving support to the stability of the general economy necessitates a continuation of the purchase of Treasury bills begun in the reserve week ending August 19. An immediate program of Treasury bill purchases is, therefore, recommended commencing with the reserve week ending August 26 and continuing at least until the policy can be reviewed at the next meeting of the executive committee of the Open Market Committee. It is proposed that new purchases of Treasury bills should be made at the rate of $30 million to $60 million a week, with the size of purchases to be varied to the extent that the Treasury reduces the average size of its balances at the Federal Reserve Banks or to the extent that repurchase agreement transactions might be temporarily substituted for outright Treasury bill purchases. The result of these operations might be to supply more reserves to the market than are immediately necessary for seasonal credit expansion requirements, but as has been previously set out, offsetting measures can be easily instituted should subsequent events so dictate. However, considering the state of the economy and the fact that the banks are indicating a desire to strengthen their liquidity via increasing their investments in short-term U.S. Government securities, it does not seem likely that an easier money policy will threaten the use of new reserves as a basis for an unwise expansion of credit.

Moreover, the new reserves that would be supplied by way of the proposed program would tend to strengthen the Government securities market at a period of important Treasury financing by permitting the banks enough elbow room for appropriate participation in this operation. The fiscal benefits resulting should also set the stage for subsequent Treasury borrowings without at the same time compelling the Federal Reserve System to sacrifice any important degree of credit restraint. The policy as above proposed also recognizes that as substantial additional reserves must be made available during the fourth quarter of the year, it would be advisable to supply them on a gradual basis that would be least disturbing to market price structures rather than to be compelled to provide them abruptly in large amounts at later dates. Where the gradual approach of supplying new reserves may result in periods of temporary market ease, it can be expected that such conditions will be automatically corrected as the seasonal demand for credit gathers momentum in the later months of the fall. In the event automatic correction of any undue market ease should not be forthcoming, more positive corrective measures can be taken of the sort that have been previously reviewed.

An open market policy placing first emphasis on the needs of the general economy requires a further look into the future. In that regard prospective Federal budgetary improvement by way of lower expenditures will tend to reduce the stimulus to the economy that is implicit in Federal expenditures. Therefore, it can be argued that an advance relaxation of credit via easing bank reserve positions will stand to encourage a freer use of credit in the civilian sector of the economy at a time that compensatory action of this nature might prove to be highly desirable. The risks of waiting to ease credit until there is palpable need to do so as against the risks that an earlier easing of credit might have inflationary consequences suggests that open market policy should make the second rather than the first choice.

Mr. Sproul requested that Mr. Young review the economic and credit situation so that the suggestions made by Mr. Mills could be considered in the light of a report on current developments.

In his comments, Mr. Young summarized economic activity substantially along the lines of a memorandum prepared by the staff under date of August 21, 1953 in which it was stated that record levels of aggregate output and employment attained in the second quarter of 1953 have generally been maintained thus far in the current quarter; that the situation continued to be characterized by over-all stability in prices and activity and by considerable selectivity in developments in particular lines; and that whether this is a period of formation of forces for further uptrend or for some downward readjustment can not yet be clearly read from current business indicators.

Mr. Vardaman withdrew from the meeting during Mr. Young's statement.

Mr. Youngdahl supplemented Mr. Young's comments with a review of the banking and credit situation. In his remarks, Mr. Youngdahl said that there might be little change in the reserve position of banks over the two week period ending September 2 but that in the statement week ending September 9, currency out-flow associated with the Labor Day Holiday could be expected to draw on reserves of banks.

Mr. Sproul suggested that with this background the committee proceed to a discussion of the program for open market operations during the next two or three weeks, adding the comment that he came out at about the same position as Mr. Mills with respect to operations during this period. Mr. Sproul then made a statement substantially as follows:

1. General economic conditions and the near term outlook continue to reflect a broad vigorous horizontal movement at a high level, and with stability in the broader price indices. In other words we are not combatting inflation or deflation at present.

2. This situation suggests a continuance of a policy of meeting seasonal and growth demands for additional bank reserves during the rest of the year, without permitting the reserve situation to become sloppy, inviting speculative or fringe uses of credit.

3. We can not be so certain of the accuracy or timing of our interim estimates of the need for bank reserves, however, as to encourage faith in too fine adjustments. We also have sufficient leeway in terms of approximate needs over the whole of the remainder of the year to permit us some margin of error now. In terms of open market operations, I would like to avoid errors, if possible, which create the actuality or the prospect of tighter credit conditions and higher rates in the fall. I would make my errors on the side of ease rather than restrictions and hope to correct them later if necessary.

4. This would be sound credit policy in terms of the present state of the economy. It would also fit in well with the Treasury's problems of debt management, involving as they do an unfortunate combination of large and frequent refundings and further new money borrowing at a time of high level business activity and private and "municipal" capital investment.

5. The fact that member bank borrowings have again reached a substantial figure and have been roughly equal to excess reserves for some weeks, and that banks have been selling Government securities as their loans have increased, confirms me in the opinion that such a course does not seriously risk a revival of inflationary pressures from the credit sector, and does guard against unnecessary credit restraint, whenever our economic balance is precarious.

Mr. Sproul went on to say that his principal reservation as to Mr. Mills' position would be with respect to naming any particular amount of securities to be purchased from week to week. Factors which might affect the reserve position of banks such as changes in the Treasury balance, currency, and gold could not be so accurately estimated from week to week as to enable the committee to say whether purchases should be at a specified rate. For this reason, he would hesitate to give an instruction that any specific amount such as $30 to $60 million a week should be put into the market, and would prefer that the general instruction indicate that the present position should be continued and that, in putting funds into the market, any errors that might be made should be on the side of liberality. Certainly, Mr. Sproul said, the System should not be taking funds out of the market in this period.

Mr. Robertson said that he would go along with an instruction to the effect that conditions should be kept on an even keel and that in making adjustments in the System account any errors should be on the liberal side of supplying reserves. He would not wish to have the instruction imply that operations should create any additional ease in the market.

Mr. Sproul stated that he would wish to avoid any indication that funds automatically should be put into the market to create additional ease.

Mr. Mills said that he would be more didactic, that within reason he would introduce new reserves, that he believed very strongly that the manager of the account should be thinking in terms of weighting operations on the side of liberality, and that he should anticipate circumstances that might call for additional reserves rather than letting the need for reserves arise before they were provided. The suggestions of Messrs. Sproul and Robertson, he indicated, would simply continue the present policy. Mr. Mills said that he could not reconcile his thinking to this view, that the committee knew that as the fall season developed it would be necessary for the System to put additional reserves into the market, and that the question was whether it would be more disturbing to the market to make the addition in a lump sum or whether it would be preferable to introduce the reserves that would be needed on an ascending basis. While he would leave to the discretion of the manager of the account the details of operations, Mr. Mills said, he felt it would be desirable for the committee to take a positive position that additional reserves should be introduced rather than to allow the market to become too tight and then act to supply reserves.

Mr. Fulton stated that he agreed with the latter statement of Mr. Mills, that is, that it would be desirable to avoid permitting the situation to become too tight. Mr. Fulton would lean toward the side of ease.

Mr. Mills again referred to his suggestion that purchases for the System account be at the rate of $30 to $60 million a week, commenting that additions of reserves in such amounts would be extremely modest in relation to the total reserve structure. In response to a question from Mr. Rouse as to whether he would distinguish between outright purchases and acquisitions of securities under repurchase agreements, Mr. Mills said that he very definitely would prefer that additions of reserves be made in the more permanent form of outright purchases of securities, although he felt repurchase facilities also should be made freely available.

Mr. Sproul said that there appeared to be general agreement with the policy of providing the reserves necessary for growth and expansion of the economy during the remainder of this year and that any errors which might be made from week to week should be on the side of ease rather than restriction. The only question of agreement was whether the instruction to the Federal Reserve Bank of New York should be such that the Manager of the System Account would begin to anticipate the need for reserves over the remainder of this year through making weekly purchases in terms of some such figure as that suggested by Mr. Mills, or whether the instruction should be to continue the present program with emphasis on the side of ease rather than restraint, carrying on operations so as to maintain the present firmness, confidence, and what appeared to be a satisfactory condition in the money market.

Mr. Mills stated that he disliked setting amounts as much as anybody but that if purchases were delayed until it became necessary to make large additions to reserves, such purchases might fall at the time payment was being made for the Treasury's new offering of securities and such a situation could again expose the System to the charge of adapting policy to Treasury needs rather than with primary regard to the economic and monetary situation.

Mr. Sproul indicated that the Treasury's refunding announcement might be anticipated on August 28 or 31, that the books would probably be open from about September 2 to September 4, and that after September 2 it was expected that the market would be gaining reserves. Under all the circumstances, he did not feel that there would be much basis for accusing the Federal Reserve of rigging the market to suit the Treasury's needs or of failing to do something which the System should do in order to make the Treasury's position easier. Mr. Sproul then inquired of Mr. Mills whether he would agree with an instruction to the Federal Reserve Bank of New York to conduct operations for the System account so as to continue the present position and to err on the side of ease if there were question as to whether funds should be put into the market, with the understanding that the System would continue to make repurchase agreements freely available.

Mr. Mills stated that he was sure that such an instruction would reflect the spirit of the executive committee and that he would accept it.

Thereupon, upon motion duly made and seconded, the executive committee voted unanimously to direct the Federal Reserve Bank of New York until otherwise directed by the executive committee:

(1) To make such purchases, sales, or exchanges (including replacement of maturing securities and allowing maturities to run off without replacement) for the System account in the open market or, in the case of maturing securities, by direct exchange with the Treasury, as may be necessary in the light of current and prospective economic conditions and the general credit situation of the country, with a view (a) to relating the supply of funds in the market to the needs of commerce and business, (b) to avoiding deflationary tendencies without encouraging a renewal of inflationary developments, and (c) to the practical administration of the account; provided that the total amount of securities in the System account (including commitments for the purchase or sale of securities for the account) at the close of this date shall not be increased or decreased by more than $500 million;

(2) To purchase direct from the Treasury for the account of the Federal Reserve Bank of New York (with discretion, in cases where it seems desirable, to issue participations to one or more Federal Reserve Banks) such amount of special short-term certificates of indebtedness as may be necessary from time

to time for the temporary accommodation of the Treasury; provided that the total amount of such certificates held at any one time by the Federal Reserve Banks shall not exceed in the aggregate $500 million.

Mr. Sproul stated that he understood that he and Mr. Mills were to attend a meeting with the Secretary of the Treasury at 2:30 p.m. this afternoon, at which there would be a discussion of the Treasury's plans for refunding the 2 per cent bonds maturing September 15 in the amount of $7,986 million. He stated that, having in mind that the committee no longer made any recommendations either in writing or orally as a committee on the question of what the Treasury should do, he would appreciate any comments or suggestions which would help in advising the Treasury of what credit policy is goind to be, as well as suggestions as to what either he or Mr. Mills might say as individuals in expressing views with respect to the Treasury financing.

There followed a general discussion of the types of Treasury securities that might be offered in the current refunding. During the discussion, Mr. Robertson stated that he could see no factors in the credit situation that would lead him to believe that there were compelling reasons, from the point of view of credit policy, for preferring any specific type of offering, and that such decision should be left entirely to the Treasury.

Mr. Sproul suggested that this might be indicated by saying to the Secretary of the Treasury that, from the standpoint of credit policy, there appeared to be no evident need to make a decision one way or the other, that the decision would be for the Treasury to make in terms of debt management.

There was unanimous agreement with this suggestion as well as with Mr. Sproul's statement that any views which either he or Mr. Mills might express as to other aspects of the Treasury's refunding would not reflect opinions of the executive committee and would not be based on credit policy but would be simply individual opinions with respect to the Treasury's problem.

It was agreed that the next meeting of the executive committee should be held at 10:30 a.m. on Tuesday, September 8, 1953.

Thereupon, the meeting adjourned.

Winfield W. Riefler
Secretary