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, D. C., on Tuesday, June 13, 1950, at 2:15 p.m.

PRESENT: Mr. McCabe, Chairman
Mr. Sproul, Vice Chairman
Mr. Davis
Mr. Draper
Mr. Eccles
Mr. Erickson
Mr. Peyton
Mr. Szymczak
Mr. C. S. Young

Mr. Morrill, Secretary
Mr. Carpenter, Assistant Secretary
Mr. Thomas, Economist
Messrs. Peterson, Stead, and John H. Williams, Associate Economists
Mr. Rouse, Manager, System Open Market Account
Mr. Thurston, Assistant to the Board of Governors
Mr. Riefler, Assistant to the Chairman, Board of Governors
Mr. Sherman, Assistant Secretary
Mr. Ralph Young, Director, Division of Research and Statistics, Board of Governors
Mr. Youngdahl, Chief, Government Finance Section, Division of Research and Statistics, Board of Governors
Mr. Arthur Willis, Special Assistant, Securities Department, Federal Reserve Bank of New York

Messrs. Williams, Gidney, Gilbert, and Leedy, alternate members of the Federal Open Market Committee

Messrs. Leach, McLarin, and Earhart, Presidents of the Federal Reserve Banks of Richmond, Atlanta, and San Francisco, respectively

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

Upon motion duly made and seconded and by unanimous vote, the minutes of the meetings of the Federal Open Market Committee held on February 28 and March 1, 1950, were approved.

Upon motion duly made and seconded and by unanimous vote, the actions of the executive committee of the Federal Open Market Committee as set forth in the minutes of the meetings of the executive committee held on March 1, April 12, and May 3, 1950, were approved, ratified, and confirmed.

Before this meeting there had been sent to each member of the Committee a copy of a report of open market operations prepared at the Federal Reserve Bank of New York covering the period from March 1, 1950, to June 7, 1950, inclusive. Mr. Rouse commented briefly on this report and also on a supplemental report covering commitments executed for the System account during the period June 8 to June 12, 1950, inclusive. Copies of both reports have been placed in the files of the Federal Open Market Committee.

Upon motion duly made and seconded and by unanimous vote, the transactions in the System account for the period February 28, 1950, to June 12, 1950, inclusive, were approved, ratified, and confirmed.

Chairman McCabe reported briefly on developments since the last meeting of the Committee referring particularly to the letter sent to the Secretary of the Treasury, pursuant to action of the executive committee of the Federal Open Market Committee, under date of May 25, 1950, a copy of which had been sent to each member of the Committee. He stated that up to the present time no reply to that letter and no comment with respect to the recommendations contained in it had been received from the Treasury Department.

There followed a discussion of the relationship of Treasury financing to System credit policy during which Mr. Sproul made a statement substantially as follows:

> System credit policy is restricted to a modest policy so far as money rates are concerned. The older method of substantial changes in rates is not practicable or necessary in this situation. Since our policy must be a modest one, it should be a timely and flexible one. We have tried to base policy in the past on the whole situation and not on one or a few indicators. There has been no change in our policy since we changed last fall from a policy of ease to one of neutrality. Meantime there has been a substantial change in the economic situation, in business sentiment, in private capital expenditures, in inventory accumulation, and in prices. On the other hand, bank credit has declined about seasonally during the spring, and the Federal Reserve Banks and commercial banks have moved about $3 billion of Government securities into nonbank hands. There is the question which was discussed during the spring of whether, in order to maintain the economy at a sufficiently high level of production to absorb the increasing labor force, we have to keep some element of stimulation in it.
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> If we were convinced that we are experiencing a balanced expansion in durable and nondurable goods we would need to do nothing about it. But I do not think we are having a balanced expansion. It is based too much on a high level of activity in housing and automobiles, aided by too easy terms for mortgage financing and consumer credit. In these circumstances, the contribution of a modest credit policy should be to try to restrain a too rapid increase until the whole economy is in better

balance. That calls for a firming of short-term rates by 1/8 per cent as soon as the Treasury's July 1 financing is out of the way. There should be some further decline in prices of long-term Governments and if we come to a situation when we are faced with the decision whether to let long-term bonds go below par, I would let them go below par. The situation is very different from the one existing the last time we faced this question.

The Treasury needs for new money have been reduced to about $1.8 billion for the fiscal year with only a small amount needed in the third quarter of this calendar year. In this situation there should be no embarrassment to the Treasury in such firming of interest rates as we are talking about. Such a policy would contemplate breaking a 1-1/4 per cent one-year rate early in July. It would be an indication of policy to the money market and would facilitate some downward movement of prices in the long-term market. It should be followed quickly by some increase in discount rates which would be a signal to the whole financial community and to the public that there has been a change in our policy in the light of the changed business and credit situation. We should continue to press for the Treasury getting additional money so far as possible from nonbank investors. In the circumstances, it makes no difference whether the money comes from a marketable or a nonmarketable bond but we should emphasize the desirability of it coming from nonbank sources.

In the ensuing discussion Mr. C. S. Young raised the question whether an increase in margin requirements would be desirable in view of recent rises in prices of stocks and stock market activity.

Chairman McCabe stated that the Board had considered this matter at a meeting this morning and that it had come to the conclusion that no change in margin requirements was desirable at this time. At his request there were distributed copies of a confidential memorandum prepared in the Division of Research and Statistics of the Board of Governors under date of June 8, 1950, with respect to the question of margin requirement policy.

There then followed a visual presentation of the economic situation by members of the staff of the Board's Division of Research and Statistics.

Following the visual presentation, Mr. Thomas made a statement regarding what the analysis signified in terms of Federal Reserve policy. He stated that recent developments appeared to have many of the aspects of a boom, that a substantial volume of business capital expenditures had been taking place and some contraction might now be expected, that increased consumer buying of consumer durable goods and housing was proceeding at a rate which probably would not be sustained, and that rises in prices of an unexpected and most alarming character had taken place during the last four months. Credit expansion, he said, had taken place in real estate, consumer credit, and the stock market at a rate more rapid than at any other time in the postwar period, and if business credit should increase even at a seasonal pace the overall expansion would be almost unprecedented. Mr. Thomas also said that, reflecting the policy of selling Government bonds from the System account, bank credit in U. S. Government securities had contracted thus far this year, that that had had a stabilizing influence, but that if the trend should be reversed accompanying a continuation of the expansion of credit in other fields there would be cause for alarm. He added that the rise in prices of real estate and commodities of the type now occurring and under conditions now existing was a clear indication of an unhealthy situation, and the expansion in credit had been sufficiently broad to justify the use of general quantitative powers of credit restraint without emphasis on selective credit controls.

After discussing existing limitations on Federal Reserve actions, Mr. Thomas suggested policies which might be considered by the Committee. These included the purchase of short-term securities more reluctantly with consequent rises in short-term rates after July 1, an increase in the discount rate of the Federal Reserve Banks, a recommendation to the Treasury that new money to finance the Government deficit be obtained through the issuance of a non-marketable bond, and that securities maturing in September be refunded with an intermediate-term bond. He added that sales of long-term bonds for the System account probably should be discontinued in the event the Treasury issued a nonmarketable long-term bond and that in the event of a decline in bond prices the policy of the System should be to maintain orderly markets but avoid rigid support of prices.

There followed a discussion of the economic situation during which Mr. John H. Williams stated that he felt the present offered an almost unparalleled opportunity for the System to do something to follow up the statement issued by the Federal Open Market Committee on June 28, 1949, as there might never be a time when we could act with less embarrassment to the Treasury. For reasons which he outlined, he felt that nothing would be as well understood by the public or carry as much conviction as an increase in the discount rate.

Mr. Stead suggested the possibility that the estimates of employment were on the optimistic side and that in the next few months we might experience some increase in unemployment. While this might not be serious in relation to total employment, it might result in pressures for steps to counteract that trend. A related subject, he said, was the indication of lower agricultural production resulting from insect infestation which would reduce farm income, and a third weakness was the rate of increase in consumer and mortgage credit which indicated that we are sustaining a high level of consumer expenditures and incomes by a rapid increase in consumer credit. These points made him more inclined to question whether the present upsurge could be sustained.

Mr. Peterson questioned whether there was sufficient optimism in the whole economy to sustain an accelerating boom for any length of time. He suggested that there was a feeling of caution among small businessmen which would dampen the current inflationary boom.

Mr. Evans joined the meeting during the foregoing statements, having just arrived in Washington from the West.

During consideration of the suggestions that had been made earlier in the meeting concerning credit policies that might be adopted, Mr. Sproul stated that in the light of all of the factors in the situation it seemed to him that as soon as the Treasury's July 1 refunding was out of the way the System should follow a policy of bringing about a rise in short-term rates looking to an issuing rate of 1 3/8 per cent on one-year Treasury certificates in September. He felt that the increase in short-term rates would be a signal to the financial community of a change from the policy of neutrality adopted in the fall of 1949, that to make clear to the public the change in policy there should also be a prompt increase in the discount rate of the Federal Reserve Banks probably about mid-July, and that these actions should be accompanied by continuing to supply long-term bonds from the open market account although, as suggested by Mr. Thomas, the release of securities might be modified in the event the Treasury issued a long-term bond. With respect to prices of long-term Treasury bonds, Mr. Sproul did not think the Committee was now faced with the problem of whether such securities should be allowed to fall below par but that he now felt that if that question should arise during the next few weeks they should not be supported at par.

Mr. Eccles stated that he felt the first thing to do was to make every effort to induce the Treasury to finance the deficit and if possible to refund some of the maturing securities with funds obtained from nonbank investors, and that to that end the Committee should recommend to the Treasury that it issue as soon as possible a nonmarketable 15-year 2-1/2 per cent bond on a tap basis. As a part of the program, he felt that the Committee should do what it could to increase the short-term rate so that the September and October refunding of the Treasury would be done on the basis of a 1 3/8 per cent one-year certificate rate. He recognized that to be most effective an increase in short-term rates should be accompanied by a rise in the discount rate. However, he questioned whether the Federal Reserve Banks should increase the rate as soon as suggested by Mr. Sproul. Such action, he said, would increase the spread between the discount rate and the short-term rate on Government securities which would discourage the use by member banks of the discount facilities of the Reserve Banks to adjust their reserve position from week to week. While he did not anticipate that long-term bonds would decline to par in the near future, he suggested that if prices declined to around 100-1/2 the Committee review its policy before testing the market closer to par.

Mr. Evans said that he did not think at the moment that the Committee was faced with the problem of allowing long-term securities to decline below par and that should that question arise there should be another meeting of the Committee.

Comments of the other members of the Committee and of the

Presidents of the other Federal Reserve Banks indicated general agreement with the suggestion for an increase in short-term rates and continuance for the time being of the present policy of making long-term bonds available from the System account.

The meeting then recessed and reconvened on Wednesday, June 14, 1950, at 10:10 a.m. with the same attendance as at the close of the session on June 13 except that Mr. Thomas was not present.

Chairman McCabe referred to the instructions to be issued to the executive committee with respect to sales of long-term bonds from the System account and to the understanding at the meeting on March 1, 1950, that, operating under the general direction issued by the Federal Open Market Committee to the executive committee, and within the limits imposed by the terms of Treasury financing and by the necessity of avoiding a loss of confidence in the long-term Government securities market, the executive committee would continue to sell long-term securities from the System account unless and until there was a change in the business situation which made it undesirable to pursue that policy. He suggested that, in the light of the discussion at the session yesterday afternoon, the executive committee be authorized to continue to carry out that understanding until the price of the longest restricted Treasury bond reached 100-1/2, at which time sales would be discontinued and, if the market continued weak, the executive committee would be authorized to purchase such securities at declining prices as might be necessary to preserve orderly market conditions.

There was a further discussion of the timing of an increase in the discount rate at the Federal Reserve Banks and, while it was the consensus that the increase should not be made effective until the short-term market rate increased somewhat, there was no decision on the question what level in the short-term rate would call for discount rate action. Mr. Sproul thought the action could be taken about the middle of July.

Turning to the question of current Treasury financing needs, Chairman McCabe suggested that he and Mr. Sproul be authorized to supplement the suggestion contained in the letter to the Secretary of the Treasury dated May 25, 1950 by urging that the Treasury issue promptly a nonmarketable bond of the series A type, and that the question whether there should be a further written communication to the Treasury be left for determination by himself and Mr. Sproul following the meeting with the Secretary.

The foregoing suggestion was approved by unanimous vote.

In considering the general direction to be issued to the executive committee, it was suggested that there be added to the second paragraph a sentence which would provide that the authority to arrange for purchases of securities directly from the Treasury would terminate on June 30, 1950, unless the authority of the Federal Reserve Banks to effect such transactions was extended by the Congress.

With respect to the limitations contained in the direction, Mr. Rouse stated that the present limitations appeared to be satisfactory.

Thereupon, upon motion duly made and seconded, the following direction to the executive committee was approved unanimously with the understanding that the limitations contained in the direction would include commitments for the System open market account:

The executive committee is directed, until otherwise directed by the Federal Open Market Committee, to arrange for such transactions for the System open market account, either in the open market or directly with the Treasury (including purchases, sales, exchanges, replacement of maturing securities, and letting maturities run off without replacement), as may be necessary, in the light of changing economic conditions and the general credit situation of the country, for the practical administration of the account, for the maintenance of orderly conditions in the Government security market, and for the purpose of relating the supply of funds in the market to the needs of commerce and business; provided that the aggregate amount of securities held in the account at the close of this date other than special short-term certificates of indebtedness purchased from time to time for the temporary accommodation of the Treasury shall not be increased or decreased by more than $2,000,000,000.

The executive committee is further directed, until otherwise directed by the Federal Open Market Committee, to arrange for the purchase for the System open market account direct from the Treasury of such amounts of special short-term certificates of indebtedness as may be necessary from time to time for the temporary accommodation of the Treasury; provided that the total amount of such certificates held in the account at any one time shall not exceed $1,000,000,000. The direction in this paragraph will terminate on June 30, 1950, unless the authority of the Federal Reserve Banks to purchase securities directly from the Treasury is extended by the Congress.

The policy to be followed in the replacement of System maturing bill holdings was then discussed and it was agreed unanimously that no change should be made in the existing understanding that the executive committee would be guided by what would be required in the light of current conditions in the money market to carry out the general credit policy of the Federal Open Market Committee.

In connection with the ranges within which bills and certificates would be purchased by the Federal Reserve Bank of New York for the System account, it was suggested that the Federal Open Market Committee continue the existing authority to the executive committee to determine from time to time the ranges within which such purchases would be made, with the understanding, however, that after July 1, 1950, the upper limit of such ranges would be increased from 1.24 to 1.36 per cent, and that the authority would continue to be exercised within the framework of the general credit policy of the Federal Open Market Committee.

Upon motion duly made and seconded and by unanimous vote, this suggestion was approved.

A draft of a statement of policy to guide the executive committee in relation to transactions in long-term bonds, designed to conform to the views expressed in the discussions of the Committee earlier in this meeting, was presented, and after discussion was approved unanimously in the following form:

Operating under the general direction issued by the Federal Open Market Committee to the executive committee, the executive committee is authorized to continue to sell long-term securities from the System account unless and until there is a change in the business and credit situation, or the Treasury issues new securities to finance the deficit, which would make it undesirable to pursue the policy further. Should the price on the longest restricted issue decline to between 100-1/2 to 100-3/4 the executive committee would direct only such operations as were necessary to maintain orderly market conditions pending a meeting of the Federal Open Market Committee which would be called promptly to consider, in the light of the statement approved at the meeting on June 28, 1949, how far any further decline that would be brought about by market conditions would be permitted to go.

It was understood that the next meeting of the Presidents' Conference would be held in Boston on September 21 and 22 and that the next meeting of the Federal Open Market Committee and the joint meeting of the Presidents and the Board would be held in Washington on September 27 and 28, 1950, unless developments made it necessary to call a meeting of the Federal Open Market Committee before that time.

Thereupon the meeting adjourned.

Chester Morrill
Secretary.

Thomas B. McCabe
Chairman.