

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 in Washington on Wednesday, December 11, 1946, at 11:10 a.m.

PRESENT: Mr. Eccles, Chairman
Mr. Sproul, Vice Chairman
Mr. Draper
Mr. Evans
Mr. Leach

Mr. Morrill, Secretary
Mr. Carpenter, Assistant Secretary
Mr. Vest, General Counsel
Mr. Thomas, Economist
Mr. Rouse, Manager of the System
Open Market Account
Mr. Musgrave, Chief of the Government
Finance Section of the Division of
Research and Statistics of the
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
October 3, 1946, were approved.

Mr. Rouse made a brief statement supplementing the regular reports made by the Federal Reserve Bank of New York to members of the executive committee with respect to transactions in the System open market account since the last meeting of the committee and current conditions in the Government security market.

At the conclusion of Mr. Rouse's statement, upon motion duly made and seconded, and by unanimous vote, the transactions in the System account during the period from October 3 to December 10, 1946, inclusive, were approved, ratified, and confirmed.

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In connection with his statement, Mr. Rouse referred to the understanding reached at the last meeting of the executive committee that he would give notice in writing to D. W. Rich & Co., Inc., qualified as a dealer, and Chas. E. Quincey Co., qualified as a broker, that unless the extended positions in Government securities maintained by the two concerns were reduced they would be discontinued as concerns with which the Federal Reserve Bank of New York would do business for the System open market account. He said that, after consultation with counsel and after informal conferences with representatives of the concerns, letters were sent to them in accordance with the understanding of the executive committee, that the final response from D. W. Rich & Co., Inc., had not been received, but that a representative of Chas. E. Quincey Co. had stated that his firm would be glad to cooperate and that the necessary correction would be made within the course of the next 30 days.

Mr. Rouse also said that when, in accordance with the action taken at the meeting of the executive committee on June 10, 1946, he began to include in the weekly report statements with respect to the large position of the two concerns above referred to, a report was circulated in New York that the Federal Reserve Bank of New York was "after" two of the

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qualified dealers. In these circumstances, it was Mr. Rouse's suggestion that the instructions issued by the executive committee in this connection be changed to require that information with respect to the position and borrowings of individual dealers be not included in the weekly report prepared by the Federal Reserve Bank of New York but that such information be reported to the members and secretary of the executive committee in a separate weekly report.

Upon motion duly made and seconded, Mr. Rouse's suggestion was approved unanimously and the procedure approved at the meeting of the executive committee on June 10 was changed to read as follows:

The Federal Reserve Bank of New York should send to the members and secretary of the executive committee of the Federal Open Market Committee, as a supplement to the Bank's regular weekly report, a statement that during the period covered by the report the position and borrowings of individual dealers or of all dealers combined, in its opinion, had or had not been excessive as the case might be. In the event the position and borrowings of an individual dealer or of all dealers taken together were believed to be excessive, the statement should include a report of any action considered by the New York Bank, the action taken by the Bank, and the response by the dealer or dealers thereto.

Mr. Rouse then reported that the Federal Reserve Bank of New York had received a request from the Manufacturers Trust Company that it be permitted to do business with the New York Bank for the System

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open market account, but that, after having reviewed the statement of terms and conditions approved by the Federal Open Market Committee under which the New York Bank would transact business with brokers and dealers for the System account, the Trust Company had concluded that it did not wish to become a qualified dealer at this time.

At this point Mr. Thurston, Assistant to the Chairman of the Board of Governors, joined the meeting.

Following a general discussion of going rates and rate trends in the money market, reference was made to the letters sent to the Treasury on October 4 and November 12, 1946, with further regard to the program for the retirement of Government debt. The first letter was in accordance with the conclusions reached at the meeting of the Federal Open Market Committee on October 3 and the second was sent by Chairman Eccles after informal consultation with the other members of the executive committee. The two letters were as follows:

Letter of October 4, 1946

"Mr. Bartelt has asked that I give you the views of the Federal Open Market Committee with respect to the maturing November 1 certificates.

"The Committee recommends that 2 billion dollars of the issue be redeemed for cash and that 1.8 billion be exchanged into certificates. The Committee also recommends that the entire issue of 1 1/2 per cent notes be retired on December 15. According to our most recent estimates, the Treasury cash balance under this program would be ample at about 2 billion dollars at the end of the year. This estimate makes allowance for a rather large amount of December 1 certificates that might not be exchanged.

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"We feel that it is important to retire the entire December 15 note issue. If the estimates of your staff should cause you to feel that you cannot retire the amount of debt suggested above and still maintain a satisfactory cash balance, we would favor the retirement of a smaller amount on November 1, say 1.5 billion dollars, in order to make possible the retirement in full of the December 15 notes."

Letter of November 12, 1946

"Mr. Bartelt has requested the views of the Federal Open Market Committee with respect to debt retirement in December.

"The Committee reiterates its recommendation of October 4 that an exchange offer be made for the entire amount of December 1 certificates and that the note issue maturing on December 15 be retired in full. Full payment of this note issue is especially desirable because it bears an interest rate of one and one-half per cent and because partial refunding into certificates would result in having three certificate issues, all maturing within 31 days.

"On the basis of present budgetary estimates, the Committee also tentatively recommends (1) that the January 1 and March 1 certificate issues be exchanged in full, (2) that the March 15 note issue be fully paid off, and (3) that the certificate issue maturing February 1 be paid off to the extent that funds are available and are not needed to meet the March 15 retirement.

"It is estimated under this program that following the mid-December retirement, Treasury balances may temporarily drop below a billion dollars, depending largely on the amount of the December certificates that are redeemed for cash. However, the Committee feels that war loan deposit accounts should not be drawn down below a billion dollars. If any additional funds are needed for a short period to keep the balances from falling below this figure, the funds may be borrowed from the Federal Reserve Banks on special certificates under the five billion dollar direct lending provision, which was especially authorized to meet just such a temporary need.

"It is believed that under the program here proposed such borrowing from the Reserve Banks would be necessary, if at all, in a relatively small amount and for only a brief period. If Treasury needs should at any time exceed estimates and require borrowing of larger amounts for more extended periods, the Treasury always has available two additional sources of funds. It can increase the regular weekly offering of bills or the monthly issues of certificates. Accordingly, so long as the Treasury's cash receipts equal or exceed current expenditures, as presently indicated, there is no reason for maintaining large cash balances.

"This flexibility makes it possible to carry smaller balances and to retire the debt more selectively and more rapidly.

"Existing law authorizing Reserve Banks to purchase directly five billion dollars of obligations from the Treasury will expire on March 31, 1947. If its extension is recommended, as we believe it should be, there would be an advantage in having demonstrated its use in operation for expediting a more rapid and selective debt retirement program than would otherwise have been possible."

Upon motion duly made and seconded, and by unanimous vote, the letters were approved and their transmission to the Secretary of the Treasury was ratified and confirmed.

As a basis for further discussion of Treasury financing and System credit policies, there were distributed copies of the following confidential memoranda which had been prepared in anticipation of this meeting:

1. Projected debt retirement program for calendar year 1947
2. Appraisal of budget outlook for fiscal year 1948
3. Savings bond program
4. Issuance of additional long-term securities
5. Treasury bills

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The memorandum relating to the retirement program for the calendar year 1947 was read and there was a general discussion of the budget picture as set forth in the memorandum.

Reference was made to the contemplated payment by the Treasury to the International Monetary Fund in the amount of \$2,750,000,000 in March and to the expectation that \$1,800,000,000 of the payment would be financed by the use of inactive gold held in the exchange stabilization fund, that the balance of \$950,000,000 would be provided from the general fund, and that the Monetary Fund would invest in Treasury obligations approximately \$1,800,000,000, which amount would be returned to the Treasury and appear as an increase in nonmarketable debt with a resulting net gain in the Treasury's cash balance. It was stated that the Treasury was considering whether it should continue to hold the latter amount as inactive gold and there was a discussion whether this procedure would be a desirable one and in keeping with the intention of the Bretton Woods Agreements Act.

It was understood that the Division of Research and Statistics would prepare a memorandum on this point for consideration at a subsequent meeting of the executive committee.

Reference was also made to the issues of Treasury notes and bonds maturing on September 15, October 15, and December 15, 1947, and the steps that might be taken in connection with the refinancing of these issues.

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At the conclusion of the discussion, upon motion duly made and seconded and by unanimous vote, the following letter to the Secretary of the Treasury was approved with the understanding (1) that the letter would be sent immediately so that it would be available at the Treasury tomorrow when a decision was to be made with respect to the January maturity of Treasury certificates, (2) that a copy of the letter and the first two memoranda listed above would be sent to the Presidents of all of the Federal Reserve Banks, and (3) that Mr. Thomas would send copies of the two memoranda to the heads of the Research Divisions of the respective Federal Reserve Banks:

"The executive committee of the Federal Open Market Committee, after discussion of the debt retirement outlook for the early months of 1947, wishes to repeat the recommendations contained in the letter which I sent you on November 12, 1946, that the January 1 and March 1 certificate issues be refunded in full and that the March 15 note issue be paid off in full.

"It now appears that it will be possible, in addition, to pay in cash from 1.5 to 2 billion dollars of the certificate issue maturing February 1, and a tentative recommendation is made that this be done looking toward a total redemption of about 4 billion dollars during the first three months of the calendar year 1947. This recommendation for the February 1 retirement will be reviewed by the committee early in January with a view to communicating with you again at that time."

Thereupon the meeting recessed and reconvened at 2:10 p.m.

with the same attendance as at the beginning of the morning session.

Following the reading of the memorandum which discussed the experience with the United States savings bond program since V-J Day, possible lessons to be learned from the recent savings bond policy in

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Canada, and what might be done in this country to revitalize the sale of savings bonds, there was a general discussion of the part that savings bonds might be expected to take in the future financing program, the kind of organization that should be used in connection with sales of savings bonds, and what should be done to make these securities more attractive particularly to the small saver. It was pointed out that \$426,000,000 of savings bonds would mature in 1947 and that, therefore, it was necessary that the Treasury reach a decision fairly soon as to what its policy would be with respect to the securities to be offered in exchange for the maturing obligations.

There was agreement that a memorandum should be prepared containing suggestions that might be made to the Treasury on this subject and that the memorandum should be considered at the next meeting of the executive committee. It was the consensus that the memorandum might suggest that the Treasury offer the choice of exchanging maturing savings bonds for (1) a new Series E savings bond, or (2) a 10-year registered coupon bond redeemable on call at par with interest at the rate of 2-3/4 per cent payable annually, it being understood that the present annual limit of \$3,750 on the purchase of Series E savings bonds would not apply to these exchanges.

The memorandum relating to the issuance by the Treasury of additional long-term securities was then read. The memorandum discussed the questions (1) whether such securities were needed in order

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to prevent a decline in the long-term rate, (2) whether they could be helpful in shifting debt out of the banking system, and (3) whether they would serve to prevent inflationary pressures in other investments.

After consideration of these and other questions involved in a decision whether additional long-term securities should be issued, it was understood that Messrs. Sproul and Rouse would prepare a revised memorandum on the subject and send it to the members of the committee for their consideration.

Chairman Eccles stated that, while the question of the action to be taken by the Federal Open Market Committee with respect to the discontinuance of the posted rate on Treasury bills was not an urgent one as long as the current retirement program of the Treasury was in effect, the posted rate had little if any significance under present conditions and should be discontinued. He also said that to replace the System's holdings of maturing bills with higher rate bills would raise the question whether the franchise tax should be reenacted or some other solution found for the disposition of the large earnings of the Federal Reserve Banks, that the franchise tax proposal would undoubtedly raise a number of other questions, and that he did not believe it would be acceptable to the Treasury for the reason that the higher rate on bills would add to the cost of Government debt while any funds received by the Treasury from a franchise tax would be covered into general receipts rather than used to reduce such cost.

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It was Mr. Sproul's view that it would be less difficult to bring about the enactment of a satisfactory franchise tax than it would be to explain the present procedure under which dealers bid for Treasury bills with the understanding that they will be resold to the System. He also suggested that the first step that the Federal Open Market Committee might take would be to arrange for a direct exchange of the System's holdings of maturing bills for new 3/8 per cent bills and that at the proper time thereafter a second step could be taken to discontinue the posted rate on bills and to seek the reenactment of a franchise tax.

Various alternatives to the steps suggested by Mr. Sproul were discussed and there was agreement that the whole matter should be discussed informally with the Treasury before any action was taken by the Federal Open Market Committee. There was also agreement that Messrs. Sproul and Rouse would prepare a memorandum on the subject, that a memorandum would be prepared at the Board of Governors, and that copies of the two memoranda would be sent to the members of the executive committee for consideration at a meeting to be held in Washington on January 10, 1947. It was understood that, immediately following the meeting on January 10, Chairman Eccles would seek an appointment for him and Mr. Sproul or possibly for all the members of the executive committee to meet with the Secretary of the Treasury to discuss the conclusions of the executive committee, following which the matter would be taken up with the members of the full Committee.

Upon motion duly made and seconded, and by unanimous vote, the executive committee directed 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, either in the open market or directly from, to, or with the Treasury, as may be necessary in the practical administration of the account or for the purpose of maintaining an orderly market in Treasury securities and a general level of prices and yields of Government securities which will support the Treasury issuing rates of $7/8$ per cent for one-year certificates and $2-1/2$ per cent for 27-year bonds restricted as to ownership; provided (a) that the total amount of securities in the account at the close of this date shall not be increased or decreased by more than \$750,000,000 exclusive of bills purchased outright in the market on a discount basis at the rate of $3/8$ per cent per annum and bills redeemed at maturity, and special short-term certificates of indebtedness purchased for the temporary accommodation of the Treasury pursuant to paragraph (2) of this direction, and (b) that this paragraph shall not limit the amount of Treasury bills purchased pursuant to the direction of the Federal Open Market Committee issued under date of March 1, 1945, or the redemption of such bills;

(2) To purchase direct from the Treasury for the System open market account 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 \$750,000,000; and

(3) Upon approval by a majority of the members of the executive committee, which may be obtained by telephone, telegraph, or mail, to make such other purchases, sales or exchanges for the account as may be found to be desirable within the limits of the authority granted to the executive committee by the Federal Open Market Committee.

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In taking this action, it was understood that the limitations contained in the direction included commitments for purchases or sales of securities for the System account.


Reference was made to the fact that in recent years the Federal Open Market Committee had followed the practice of having a meeting of the old Committee on February 28 and a meeting of the new Committee on March 1 of each year, and that inasmuch as March 1, 1947, fell on Saturday there was a question of dates to be set for these meetings next year. It was agreed that it would be desirable for the meetings of the Presidents' Conference to be held during the first part of the week beginning February 24 with the understanding that the meetings of the Federal Open Market Committee would be held on Friday, February 28, and Saturday, March 1.

Thereupon the members of the staff withdrew and the meeting continued in executive session for the purpose of discussing informally the procedures of the committee, including that followed in the submission of the views of the executive committee and the full Committee to the Treasury.

At the conclusion of the executive session the meeting adjourned.

Approved:


Chairman.


Secretary.