

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 Thursday, May 20, 1948, at 9:30 a.m.

PRESENT: Mr. McCabe, Chairman
Mr. Sproul, Vice Chairman
Mr. Eccles
Mr. Szymczak
Mr. Williams

Mr. Morrill, Secretary
Mr. Carpenter, Assistant Secretary
Mr. Vest, General Counsel
Mr. Thomas, Economist
Mr. Rouse, Manager of the System
Open Market Account
Mr. Riefler, Assistant to the Chairman
of the Board of Governors
Mr. Smith, Economist, Government Finance
Section, Division of Research and
Statistics, Board of Governors
Mr. Arthur Willis, Special Assistant,
Securities Department, Federal Reserve Bank of New York

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the executive committee held on April 21, 1948, were approved.

Upon motion duly made and seconded, and by unanimous vote, the transactions in the System account as reported to the members of the executive committee for the period April 21 to May 19, 1948, inclusive, were approved, ratified, and confirmed.

Upon motion duly made and seconded, and by unanimous vote, the letter sent to the Secretary of the Treasury under date of April 26, 1948, in accordance with the understanding reached at the meeting of

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the executive committee on April 21, 1948, was approved and its transmission to the Treasury was ratified and confirmed.

Chairman McCabe reviewed briefly the discussions which he and Mr. Sproul had with the Secretary and other representatives of the Treasury on April 28 and May 12, following which the Treasury reached a decision to refund securities maturing in June and July with 1-1/8 per cent Treasury certificates.

In the discussion of the Treasury decision it was noted that, while the Federal Advisory Council apparently was unanimous in the opinion expressed to the Board of Governors that the rate should be raised in connection with the June financing, two members of the Council, who were also members of the Committee on Government Borrowing of the American Bankers Association had, as individual members of that Committee, advised the Secretary against the increase. The point was also brought out that apparently the Secretary felt that if the rate were raised at this time it would not be as effective as at some future time when if inflationary pressures were increased the rate could well be raised.

Mr. Szymczak stated that the action of the Treasury did not foreclose action by the Federal Reserve System towards increasing the short-term rate in the market between now and September so that the refunding of securities maturing in September and October would be at a 1-1/4 per cent rate.

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In a discussion of the action that might be taken in that connection, Mr. Sproul suggested that until the July refunding was completed the System should sell from its open market account to the extent possible without interfering with the success of the refunding operations. He thought that, if the market should decline during that period to the existing support levels, consideration should be given to dropping some of the support prices to the extent that that could be done without affecting the refunding adversely. After the first of July, he said, and if the situation at that time appeared to warrant the action, steps could be taken to move up the short-term market rate, and to adjust other rates accordingly, in anticipation of an increase in the certificate rate to 1-1/4 per cent in September. He also suggested that, if the inflationary movement seemed to be getting out of hand prior to September, consideration should be given to increasing the discount rate to 1-1/2 per cent, but that otherwise the rate should not be raised until after the increase in the short-term rate to 1-1/4 per cent. He added that the increase in reserve requirements of central reserve city banks should be deferred until such time as the increase would have some effect on a developing inflationary situation. He also said that the Treasury could be advised that the "exposure" to further inflationary pressures had been increased by the continuation of the 1-1/8 per cent rate in connection with the June and July refunding and that the Federal Open Market Committee had in

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mind that after the July refunding had been successfully completed it might be necessary to take the actions outlined above in order to discharge its responsibilities.

As a collateral matter, Mr. Sproul referred to the suggestion contained in the letter of April 26, 1948, to the Treasury that a new series of savings notes be issued with an adjusted scale of rates. He said that the action on the new issue had been deferred for some months pending a decision on the short-term rate, that the new issue should not be delayed any longer, and that it should be offered with a scale of rates which would be closer to existing short-term rates and designed to reverse or at least offset the present drain on the Treasury resulting from redemptions of savings notes in excess of purchases. He also suggested that it would be helpful in the savings bond campaign which was now in progress if the Treasury would increase the limit on the amount of F and G bonds that could be purchased for pension fund investment.

In a discussion of Mr. Sproul's suggestions and of the effect on the market of the decision of the Treasury to continue the 1-1/8 per cent rate, Mr. Rouse stated that the current prices of Government bonds were well above present support prices and that this week, when there was a sharp rise in quotations with limited volume and no supply in the market, the Federal Reserve Bank of New York began to make bonds available from the System account.

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He also said that bonds had been made available by reason of a selling order from the Treasury for the account of the Federal Deposit Insurance Corporation. While this action, he said, tempered the movement, there were indications that it might be resumed and it was his feeling that any real demand that developed should be partially filled by sales from the System account for the purpose of absorbing as large an amount of bank reserves as possible without completely stopping any rise that otherwise might take place.

It was made clear during the discussion that any decision with respect to an increase in the short-term market rate prior to September should be reached only after consultation with the Treasury, and Mr. Eccles questioned whether the System should take such action over the objections of the Treasury even though the Committee felt strongly that the short-term rate should be increased. On the matter of sales of securities from the System account to temper a rise in bond prices, Mr. Eccles suggested that, since it would not be possible for some weeks to increase the short-term rate, which was the most satisfactory way under present conditions to prevent a decline in the long-term rate, the System should not sell long-term securities for the purpose of achieving the same result.

Mr. Sproul expressed the opinion, in view of the discussion over the past two or three months during which there appeared to be general agreement as to the desirability of an increase in the

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short-term rate, but with a difference on the part of the Treasury as to the timing of the increase, that if the conditions foreseen by the Committee justifying an increase in the short-term rate were to develop, the Treasury would be in accord with a decision by the Committee to lower the support prices in the short-term market. As to the question of sales of bonds from the System account, Mr. Sproul said that there were two considerations involved, first, stability of the Government security market and, second, the desirability in the present situation of selling securities whenever that could be done in order to absorb as large an amount of bank reserves as possible.

Mr. Szymczak suggested that the questions before the Federal Open Market Committee were the actions to be taken before July 1 and the policy to be followed after the July refunding had been completed.

Chairman McCabe expressed the opinion that any discussions before the middle of June with the Treasury as to what should be done after July 1 would be premature.

Mr. Rouse stated that, in the absence of other instructions from the executive committee, the Federal Reserve Bank of New York would convert the System's holding of June and July maturities into the new refunding certificate. All of the members of the executive committee indicated agreement that that should be done.

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In a discussion of the next meeting with representatives of the Treasury, there was agreement that if, at the meeting of the Federal Open Market Committee to be held immediately following this meeting, there should be agreement that the short-term market rate should be increased to 1-1/4 per cent by September and in subsequent discussions there were objection by the Treasury to that action, it would be necessary for the full Committee to meet again and issue new instructions to the executive committee.

Mr. Eccles suggested that the full Committee might authorize the executive committee, after conferring with the Treasury and if conditions continued to justify the action, to take such action as might be necessary to increase the short-term rate to 1-1/4 per cent so that the September refunding would be done at that rate, it being understood that if the Treasury objected to that action another meeting of the full Committee would be called. The other members of the committee indicated agreement with Mr. Eccles' suggestion.

Following a further discussion of the effect in the market of sales of long-term securities from the System open market account as proposed by Messrs. Sproul and Rouse, the meeting recessed to reconvene following the meeting of the Federal Open Market Committee.

Approved:

Norman B. McCall
Chairman.

Orestes Morrie
Secretary.