

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 Tuesday, September 25, 1951, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Sproul, Vice Chairman
Mr. Szymczak
Mr. Williams
Mr. Powell, Alternate Member

Mr. Carpenter, Secretary
Mr. Sherman, Assistant Secretary
Mr. Thomas, Economist
Mr. Rouse, Manager, System Open Market Account
Mr. Riefler, Assistant to the Chairman, Board of Governors
Mr. Young, Director, Division of Research and Statistics, Board of Governors
Mr. Solomon, Assistant General Counsel, Board of Governors
Mr. Youngdahl, Chief, Government Finance Section, Division of Research and Statistics, Board of Governors
Mr. Leach, Economist, Division of Research and Statistics, Board of Governors
Mr. 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 August 27, 1951, were approved.

The Secretary referred to the minutes of the meeting of the executive committee held on August 8, 1951, which were approved at the meeting on August 27, 1951, stating that Mr. Sproul had been on the West Coast at the time those minutes were approved and that, upon his return, he had asked that the wording of his statement on page 6 of the

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minutes be changed so that the first part of the last sentence on the page would read "Much depends on the rate of increase in defense expenditures..." rather than "Much depends on the rate of increase in the rate of expenditures..."

The foregoing change in the minutes of the meeting of the executive committee on August 8, 1951, was approved unanimously.

Mr. Rouse presented and commented upon a report prepared at the Federal Reserve Bank of New York covering open market operations for the System open market account during the period August 27 to September 20, 1951, inclusive, copies of which had been sent to the members of the committee before this meeting. He also presented a supplementary report covering commitments executed September 21 to September 24, 1951, 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 open market account as reported to the members of the committee for the period August 27 to September 24, 1951, inclusive, were approved, ratified, and confirmed.

Chairman Martin then made a statement with respect to discussions at the Ottawa Conference held last week by the North Atlantic Treaty Council and the possible bearing of those discussions on problems confronting the committee.

The Chairman then called upon Mr. Thomas who stated that there was still some uncertainty as to whether the economy was presently in a

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stage of inflation or of relative balance but that the threat of inflation was definitely present. This, he said, would indicate that the System should maintain a position of flexibility in its general credit instruments in order that it might again move against inflation should such action prove necessary. Mr. Thomas stated that it was hoped that the threat of further inflation could be managed from the credit standpoint even though there would most likely be quite an increase in bank loans during the rest of 1951 and a Federal Government cash deficit of perhaps as much as \$4 billion. This cash deficit, Mr. Thomas said, could be met in part by drawing on the Treasury cash balance and in part by borrowing. As a result, there might be an increase of as much as 7 or 8 billion dollars in the privately held money supply including nearly a billion dollars in currency. The resulting need for the reserve funds, however, might be supplied in large part by a seasonal increase in Federal Reserve float. On this basis it was estimated that additional Reserve Bank credit to be supplied either through discounts or open market operations should not exceed 1/2 billion dollars, although at times during the period larger amounts would be needed. Restraint on undue credit expansion could be sustained by supplying these needs through discounts rather than through open market operations.

In his remarks, Mr. Thomas referred to material that had been included in two memoranda prepared at the Board's offices and distributed before this meeting to members of the committee, one dated September 20,

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1951, on "Effectiveness of Recent Monetary Policies" and the other dated September 21, 1951, on "Outlook for Treasury Cash Requirements and Financing, September-December 1951". Copies of these memoranda have been placed in the files of the Open Market Committee.

Mr. Young expressed the view that the present period showed signs of the strain of a readjustment that might be much more fundamental than was commonly thought, that he was impressed with the elements on the anti-inflationary side, and that substantial future adjustments would have to be taken, particularly by dealers whose inventories were still heavy. Consumers were not in a spending mood, he said, and the outlook would depend to a considerable extent on Government expenditures for the defense program during the next few months. In sum, while the picture could turn quickly to an upswing of spending, Mr. Young felt it entirely possible that something like the present level of activity might be continued for some time.

Following a discussion of the remarks by Messrs. Thomas and Young, consideration was given to the recommendations to be made to the Treasury on refunding and new financing.

Mr. Sproul stated that there was nothing in the existing business and credit situation to indicate that a recession or depression of cumulative character would develop, that the most likely outcome of readjustments of the near-term would be a revival of creeping inflation with the prospect that higher costs rather than increased demand would furnish the

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immediate pressure in this direction. As to the credit picture, Mr. Sproul felt that the situation called for maintenance of the present restraints on credit expansion and alertness to increase such restraints if increased inflationary pressures should develop. The maintenance of existing restraints, he said, was not going to be easy with increased public borrowing over the next few months and with an increase in bank lending (for seasonal and defense needs) calling for an increase in bank reserves which the System would have to supply. The System would have to decide what was reasonable and whether to supply the needed reserves freely or to let the increased demand express itself in increased interest rates. Whatever was done, Mr. Sproul said, it was important to get the Treasury borrowing out of the way as soon as possible. He went on to say that, after reviewing the available figures and information and on the assumption that a major objective was to tap nonbank funds as a source for money, he had come to the view that the October 15-November 1 refunding of the Treasury should be done in one operation with an offering of 11-1/2 month, 1-7/8 per cent certificates dated October 15, 1951, and maturing October 1, 1952. This would be in line with the policy of maintaining the status quo so far as present credit policies, availability of reserves, and interest rates were concerned. It would help get the Treasury financing onto a quarterly basis, and it would not seem to require an excessive amount of support by the System.

As to new money which the Treasury might have to obtain this

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fall, Mr. Sproul suggested three alternatives: (1) a special offering of Treasury tax anticipation bills of about \$1-1/2 billion to be offered about October 15, 1951, and to mature in March 1952, a few days after the March 15 tax receipt date; (2) a 2 per cent 17-month note to mature in March 1953; (3) a combination offering of an 11-1/2 month, 1-7/8 per cent certificate and the 17-month note. He thought the remaining new money needed by the Treasury later in the year could be raised in a second offering in connection with the December refunding. His own preference was for the tax anticipation bill which would emphasize the temporary character of Treasury borrowing at this time, which would fit in with the Treasury revenue and expenditure outlook, and which would provide the best chance of obtaining nonbank funds. Mr. Sproul added that, because of the present congestion in the regular bill market, the Treasury should discontinue at once the additional weekly bill offerings.

Mr. Szymczak said that he agreed with the suggestion that refunding be accomplished with a 1-7/8 per cent, 11-1/2-month certificate but that he felt it would be desirable to offer an option including perhaps the 17-month, 2 per cent note suggested by Mr. Sproul or a somewhat longer issue for the purpose of probing the market and finding out where the money was. Mr. Szymczak also said that he agreed with Mr. Sproul's suggestion for eliminating the additional weekly bill offering, and that he would favor the use of the special tax anticipation bill for obtaining new money that might be required.

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Mr. Thomas stated that he and Mr. Youngdahl had been thinking of the possibility of suggesting that the Treasury open up the August 15, 1-7/8 per cent certificate which would result in a 10-month issue to mature on August 15, 1952. This would not increase the number of maturity dates since it would make use of an outstanding maturity and, from the standpoint of the money market, it would come due at a time when conditions were less likely to be tight because of seasonal demands than if the issue matured in October 1952. He also felt that an issue of a 10-month, 1-7/8 per cent certificate would call for less Federal Reserve support to assure its success than would be needed by an 11-1/2-month, 1-7/8 per cent certificate.

Mr. Thomas' suggestion was discussed, Mr. Sproul commenting that it was a good suggestion and Chairman Martin stating that while it had some merit he personally did not favor it because it would introduce a new feature in Treasury financing at a time when he felt the Treasury should wind up its current financing needs with a minimum of experimentation. The Chairman also stated that he felt the refunding should be done with a single issue rather than an option, that he did not feel the option suggested by Messrs. Sproul and Szymczak would give a real test of the market at this time, and that while opening of the August 15 certificates as suggested by Mr. Thomas might not increase the maturity dates it might be considered inconsistent with the position the committee previously had taken in urging the Treasury to follow a quarterly financing

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policy. Chairman Martin added that he favored the tax anticipation bill for new money, that there was agreement that both the refunding and new financing must be done at this time in the short-term market, and that he agreed that the additional offering of weekly bills should be discontinued.

Mr. Sproul stated that he did not feel the suggestion that the August 15 certificates be opened was inconsistent with the position taken by the committee in the past since that position had been based on the need for avoiding frequent Treasury maturities which interfered seriously with open market operations of the System. This did not necessarily call for a quarterly issue but for a reduction in the number of maturity dates.

Following a further discussion of the various alternatives offered and of the method by which the committee recommendations might be presented to the Secretary of the Treasury, Mr. Sproul suggested that the committee authorize Chairman Martin to present to the Secretary of the Treasury four alternative proposals for refunding the Treasury notes maturing on October 15 and November 1, 1951, in the amount of \$11.2 billion, such presentation to be made by the Chairman orally today and to be supplemented by a memorandum which could be placed in the Treasury files giving the committee's analysis of the situation and the reasons for its alternative suggestions. The four alternatives proposed by Mr. Sproul were:

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- (1) An 11-1/2-month, 1-7/8 per cent certificate to be dated October 15, 1951, and to mature October 1, 1952.
- (2) A combination of the certificate suggested under (1) with a 2 per cent note maturing March 15, 1953.
- (3) A 10-month, 1-7/8 per cent certificate to be dated October 15, 1951, and to mature August 15, 1952.
- (4) A combination of the certificate suggested under (3) with a 2 per cent note maturing March 15, 1953.

Mr. Sproul also suggested that in presenting these proposals the committee indicate its preference for alternative (3), i.e., a 10-month certificate to be dated October 15, 1951, and to mature August 15, 1952.

Chairman Martin stated that he personally did not wish to express a preference for a 10-month certificate to be issued October 15, 1951, to accomplish the Treasury refunding since he felt an 11-1/2-month certificate of that date was preferable for the reasons he had already stated.

Following a discussion, upon motion by Mr. Sproul, which was duly seconded, Mr. Sproul's suggestions were approved, Chairman Martin voting "no" on the action in so far as it required a preference for accomplishing the Treasury refunding with a 10-month certificate maturing August 15, 1952, rather than an 11-1/2-month certificate maturing October 1, 1952.

Secretary's note: The memorandum, which was transmitted by Chairman Martin to the Secretary of the Treasury under date of September 28, 1951, read as follows:

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"DISCUSSION OF CURRENT ECONOMIC SITUATION AND TREASURY REFUNDING
BY EXECUTIVE COMMITTEE, FEDERAL OPEN MARKET COMMITTEE,
SEPTEMBER 25, 1951

"Problems of Treasury finance for the remainder of 1951 and early 1952 were considered by the Executive Committee in the light of current and prospective economic developments with particular reference to credit demands. The recent economic situation has been marked by relative stability of prices and activity at a high level. Inflationary pressures seem to be in abeyance, notwithstanding continued increases in the rate of defense expenditures. In recent months civilian buying has not been increasing, although the level of income has continued to expand. From last spring until early September there was little credit expansion and the money market was generally in balance.

"During the next few months banking and credit developments will be affected by three important factors, the influence of which is already being felt: (1) a Treasury cash deficit of 3 to 4 billion dollars; (2) seasonal demands for bank loans, plus a probable further expansion in borrowing for defense activities of a magnitude that is difficult to predict; and (3) seasonal currency demands. These developments will result in a growth in the supply of funds in the hands of businesses and individuals that may exceed that of the period of growing inflation a year ago. Although a substantial volume of these funds will represent temporary holdings to be paid out in taxes next year, the overall expansion will be in excess of current and long-term needs and, in the absence of effective restraining action, could become an inflationary factor. The prospect for continued expansion in defense production and the resulting drain upon available supplies of goods and manpower would also add to the threat of inflation.

"In view of the recent abatement of inflationary pressures, the present situation does not call for adoption of any new and stronger measures of credit restraint. The continuing threat that inflationary pressures may reassert themselves in the near future, however, makes it undesirable to create more than a minimum volume of reserve funds during the next few weeks. During September the money market has been relatively tight, reflecting the beginning of the seasonal credit demands, as well as tax and other payments around the middle of the month. This tightness has continued, even though the Federal Reserve purchased securities and added substantial amounts to the volume of reserves. While the prospective currency and credit demands will increase the need for reserve funds during the remainder of this year,

"only small additional amounts may need to be provided through Federal Reserve purchases of securities. The prospects are that a large part of these needs will be supplied through a seasonal increase in float at the Reserve Banks, and in view of the largely temporary nature of the needs, much of the remainder might properly be met by member bank borrowing.

"Under these circumstances, the question is how the Treasury could handle its refunding and new financing with a minimum of increase in bank credit. This would require the offering of securities that would attract nonbank funds. It is clear that at present prices there is substantially no demand for medium or long-term securities. The principal potential source of demand for securities lies in business funds, which require a high degree of liquidity.

"The Executive Committee at this time concerned itself principally with the question of refunding Treasury securities maturing on October 15 and November 1. The problem of raising new funds was discussed but will be given more thorough consideration by the full Open Market Committee at its meeting on October 4 and any recommendations on that aspect will be presented after that meeting.

"The task of refunding the 11.2 billion dollars of notes maturing October 15 and November 1, of which 3.8 billion dollars are held outside of the Federal Reserve System, will be conditioned by the current state of the market for Government securities. This market is at the present in a state of congestion, reflecting the increase in the recent offerings of bills, accompanying a shortage of bank funds due to growing credit demands and a temporary shortage of corporate funds because of tax and other obligations in September. This situation has necessitated some purchases of bills and certificates on the part of the Federal Reserve in order to prevent a rise in money rates during the period of Treasury refunding. It seems likely that pressures of this nature may continue at least during the early part of October if not longer.

"Under these circumstances, the Committee agreed that short-term securities should be offered in exchange for the maturing issues. In view of the imminence of the need for new borrowing by the Treasury, the Committee also agreed that the two issues should be refunded simultaneously with the settlement date on October 15.

"With respect to particular issues to be offered in exchange for the maturing securities, the Committee gave consideration to four alternative proposals.

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"(1) The preference of the majority of the Committee is to offer to holders of the maturing securities an additional issue of 1-7/8 per cent certificates to be dated October 15 and to mature August 15, 1952. This preference is based upon the desire of the Committee, in order to facilitate Federal Reserve operations, to reduce the number of Treasury issues maturing in the latter part of next year. Since it is likely that that period may be characterized next year, as it has been this year, by active private credit demands, together with new borrowing by the Treasury, reduction in the number and amount of maturities in that period would simplify the problem of money market administration and possibly also the task of Treasury financing. In view of the fact that there is a small maturity on August 15, resulting from the September financing, the proposed issue would accomplish the purpose of reducing the number of maturities. For this reason, the proposal is considered by the Committee to be consistent with the major objective of widely-spaced maturities which underlies its previous recommendation of quarterly issues of certificates.

"(2) An alternative proposal is to offer to holders of the maturing issues a 1-7/8 per cent certificate to be dated October 15 and to mature October 1, 1952. This type of offering would fit into the quarterly pattern which the Committee has heretofore recommended and would not be out of line with the present market, although it might require some support under existing circumstances, as might also the shorter issue proposed.

"(3) and (4) The Committee also considered the proposal that a somewhat longer-term issue be offered in exchange for the October 15 and November 1 maturities. The Committee would not suggest such an exchange by itself, but the Treasury might wish to consider such an offering along with and as an option to one of the short-term securities mentioned. This type of optional offering would present an opportunity to reduce the volume of the debt maturing in 1952 and to test the market for issues maturing beyond a year. If such an option is given the Committee would suggest a 2 per cent note maturing March 15, 1953."

It was unanimously agreed that Chairman Martin would also say to Secretary Snyder that at least for the time being there should be no further increase in the weekly offering of Treasury bills.

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In a discussion of short-term rates, it was agreed unanimously that, pending completion of the refunding of the October 15 and November 1 notes, the bill rate should not be permitted to increase to a point where it would affect adversely the 1-7/8 per cent rate on the outstanding April 1 and July 1, 1952, issues of Treasury certificates.

It was further agreed unanimously that no change should be made in the understanding reached at the meeting on June 27, 1951, and continued at subsequent meetings of the executive committee that the Federal Reserve Bank of New York would not permit the price of the longest-term restricted Treasury bonds to decline below 96-3/4.

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, either in the open market or directly from, to, or 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 to exercising restraint upon inflationary developments, to maintaining orderly conditions in the Government security market, to relating the supply of funds in the market to the needs of commerce and business, and to the practical administration of the account; provided that the total amount of securities in the account at the close of May 17, 1951, shall not be increased or decreased by more than \$2 billion exclusive of special short-term certificates of indebtedness purchased for the temporary accommodation of the Treasury pursuant to paragraph (2) of this direction;

(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

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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 million.

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

It was agreed that the next meeting of the executive committee would be held immediately following the meeting of the full Committee which was to be held at 10:00 a.m. on October 4, 1951, instead of on October 3, 1951, as previously contemplated.

Thereupon, the meeting adjourned.


Secretary.