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, March 24, 1953, at 10:30 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Sproul, Vice Chairman
Mr. Erickson
Mr. Evans
Mr. Mills

Messrs. Robertson and Szymczak, members of the Federal Open Market Committee

Mr. Riefler, Secretary
Mr. Thurston, Assistant Secretary
Mr. Vest, General Counsel
Mr. Thomas, Economist
Mr. Rouse, Manager, System Open Market Account
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. Bright, Director of Research, Federal Reserve Bank of Boston

Before this meeting there had been sent to the members of the Committee a report of open market operations prepared at the Federal Reserve Bank of New York covering the period March 4 to March 19, 1953, inclusive. At this meeting Mr. Rouse presented a supplemental report covering commitments from March 20 to March 23, 1953, inclusive, and commented briefly on the reports, copies of which 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 for the period March 4 to March 23, 1953, inclusive, were approved, ratified, and confirmed.

At Chairman Martin's request, Mr. Thomas commented upon recent economic and credit developments which had been reviewed in a staff memorandum dated March 20, 1953, copies of which were distributed to the members of the committee before this meeting. Mr. Thomas stated that the general economic situation continued strong with production and incomes expanding moderately and fairly stable prices. Credit demands were still large. He said that the forcing of automobiles and other durable consumer goods upon dealers was a factor which might result in price cuts for such products later in the year and a curtailment in production. At the present time, however, there was no indication of any down turn in economic activity. Capital markets continued to reflect a very large volume of corporate and municipal issues. With respect to credit, Mr. Thomas noted that consumer and real estate loans at banks have expanded further and that following contraction earlier in the year, business borrowing had increased sharply in the past two weeks, partly as a result of borrowing for tax purposes. Mr. Thomas stated that the outlook was for continuation of a fairly tight market for the next few months unless there was a seasonal contraction in the volume of credit.

Chairman Martin asked Mr. Rouse to comment on whether recent softening in the Government securities market reflected a fundamental change in

the situation or whether it was the result of professional activity or other factors.

Mr. Rouse said that the current discussions of prospective Treasury financing which the Treasury had been carrying on with the American Bankers Association Committee on Government Borrowing and others had resulted in uncertainty in various parts of the country concerning the course of prices in the long-term market. There had been a small increase in selling of Government securities, but the situation was primarily one in which there was little buying; although bonds were not being pressed on the market, it was known that various insurance companies and others had such securities available for sale. The interest in the market presently, Mr. Rouse said, was almost entirely in the short-term sector.

Mr. Ralph Leach felt that recent developments reflected largely a professional readjustment in the market based on talk of Treasury financing. Until the Treasury made an announcement which would clarify its plans, the present uncertainty would continue. He attached significance to the recent tendency of insurance companies to look with great interest on 1-1/2 per cent five-year Treasury notes which they could obtain by conversion of 2-3/4 per cent bonds of 1975-80, since they could sell such notes at 96 or 97 thus suffering less of a loss than if they sold 2-1/2 per cent or other long-term bonds. Mr. Leach also mentioned a growing concern on the part of some investors regarding losses that might be taken on municipal bonds purchased in the past two or three years.

Following a discussion of the remarks by Messrs. Rouse and Leach, Mr. Sproul referred to the recent release of the Board of Governors giving preliminary findings of the 1953 survey of consumer finances. He asked whether press interpretations of the survey may not have overstated buying prospects during 1953, and suggested that the interpretations had been more bullish than were justified by the report. While he was not questioning either the accuracy of the figures compiled or the wisdom of releasing the data, he emphasized that consumers might well change their plans for buying if they came to realize that there was not likely to be any tax relief this year and that the Federal Government's budget situation was not going to be improved materially in the immediate future.

Chairman Martin agreed strongly with Mr. Sproul that there was a possibility of misinterpreting the data in the survey of consumer finances, adding that the Board had been aware of this possibility in releasing the data and had tried to guard against unjustified interpretations. He went on to say that it was extremely difficult to evaluate the psychology of the public at this time, that there had been a boom psychology as a result of the election last November, and that there were many signs that that psychology was continuing at present.

In response to a question from Chairman Martin, Mr. Erickson stated that, as he had reported at the meeting of the Open Market Committee on March 4, loans of banks in New England were running counter to the tendency in the United States as a whole and were continuing to increase, the largest

increases being in the textile, apparel, and leather-goods industries. Mr. Erickson said that most of the banks in New England seemed to think that loans would continue to increase. Considering the over-all economic situation, he did not feel that there was any call for an easing of credit policy at this time. On the contrary, Mr. Erickson suggested it would be desirable for the Board or perhaps for the several bank supervisory agencies acting jointly to issue some kind of a statement on the expansion of consumer credit which would be designed to bring caution to lenders in that field.

Mr. Sproul stated that one of the directors of the New York Reserve Bank at a meeting last week made a suggestion similar to that of Mr. Erickson, and, in response to a question by Chairman Martin, Mr. Sproul said that if there were indications that commercial banks were adopting the same loose practices in granting of real estate credit that seemed to be developing in consumer credit, he would think the same arguments for caution could be applied in that field. Mr. Sproul went on to say that he was a rather poor advocate of general statements of the type suggested because he did not believe too strongly in them as contrasted with the power of general credit controls. He felt general credit controls were having an effect in the consumer credit field, although perhaps not as fast as might be desired.

Mr. Robertson referred to recent discussions with the credit policy commission of the American Bankers Association, stating that that group

had appointed a committee which expected to keep in touch with developments in the consumer credit field with a view to cautioning banks whenever they appeared to be getting out of line in their general policies relating to such credit. He was hopeful that the efforts of this committee might keep banks from getting too far out of line in granting credits either to individual consumers or to finance companies.

Chairman Martin suggested that there be a discussion of the discount rate of the Federal Reserve Banks and of what the attitude of the System should be toward it during the next few weeks, including consideration of what, if any, further credit restrictions should be sought and what attempt should be made to mesh actions in this respect with debt management problems. He referred to the current very close working relations between the Treasury and the Federal Reserve, stating that any possible use of the discount rate to increase restrictions should be considered in relation to the possible offering of a long-term bond by the Treasury. The Chairman expressed concern that there might be a bullish movement during the spring months of this year followed by a sharp drop; many persons, however, did not fear such a boom development. While he was not certain what if anything the System could do to help the situation, he felt that the problem should be considered in terms of whether the System by acting now could minimize additional boom during the next three months.

With respect to the suggestion for a public statement regarding expansion of consumer credit, Chairman Martin said that, as he had indicated

previously, he believed it would be desirable if the Federal Reserve Act contained permanent authority for regulation of consumer and real estate credit. It was a different thing, however, to try to use such controls where authority was given on a temporary basis in the framework of a defense program. While he did not want credit in this field to mushroom to the point where it would destroy the whole community, he felt that any agency would be taking on a great responsibility in saying that certain terms would be unsound in a permanent defense economy such as now seemed to be developing, when individual credit grantors believed such terms were suitable. The Chairman did feel, however, that the committee should consider the possible use of general credit controls to bring further restraint in the immediate future, and he called upon Mr. Sproul for his assessment of the business picture.

Mr. Sproul's statement was substantially as follows:

"My views do not differ from the general picture presented in the staff memorandum on recent economic and credit developments distributed before this meeting or from the general comments made by Mr. Thomas. All of our reports reflect an economy running in high gear without inflation or deflation being dominant at the moment. There are disturbing signs, however, which suggest that a continued policy of credit restraint is desirable. Credit shouldn't be too readily available

(a) To finance inventory accumulation--a prop to production,
(b) To finance consumer and mortgage debt--a prop to consumption,
(c) To facilitate business outlays for plant and equipment at even higher levels than last year,
(d) To postpone desirable and corrective adjustment in production and prices, or
(e) To make it easy to grant or obtain wage increases and float them on rising prices.

"We don't want a bubble on top of a boom.

"The System has continued to pursue a policy of credit restraint since the first of this year. Roughly, up to March 11, the bank gain of reserves from declines in currency circulation and required reserves was offset by losses due to gold and foreign account transactions and reductions in System holdings of Governments. During the week ended March 18, banks gained about 800 million of reserves, which were used to reduce borrowing to about 1 billion and to increase excess reserves to about 875 million. These gains will be reversed this week as float goes down and the Treasury takes funds out of market. The banks will have to draw on their excess reserves and increase their borrowing. From then on through the second quarter, banks are likely to lose funds mainly through currency withdrawals and further losses on foreign account. There may be some offset through a reduction in reserve requirements consequent upon a seasonal decline in business loans, but there could also be a further rise in consumer loans and in investments.

"To continue our policy of credit restraint, (by keeping the banks continuously in our debt in amounts, ranging around 1-1/2 billion), but not to accentuate it, we would have to make outright purchases of Government securities during the coming quarter in an amount sufficient approximately to offset reserve losses through increased currency circulation and foreign account transactions. Temporary periods of strain can be met by repurchase agreements, but this looks like a period of continued and persistent tightness in the money market.

"If we want to tighten the situation, we could withhold funds from the market. That is when we shall run into the Treasury needs, even though we want to divorce ourselves, as far as possible, from Treasury financing requirements. The fact appears to be that the Treasury is going to have to be in the market for new money (as well as refundings) at a time of business boom when it shouldn't be a borrower. We can't ignore the situation just because it shouldn't exist. Unless inflationary pressures become stronger, we would not be justified in tightening the screws further at this time.

"If the Treasury is going to have to do some new money financing in May (as well as make some sort of a refunding offer to holders of maturing F and G bonds), and if it wants to try out the market for a long-term issue at competitive rates, I don't think we should object. From the standpoint of credit policy it seems desirable to dampen the capital market, which is now being used to feed the consumer credit market and the mortgage market as well as to support a substantial load of private capital projects. It is a Treasury decision, of course, but there would seem to be no objection from the standpoint of credit policy.

"Finally, while I think a continued policy of credit restraint is indicated and desirable, we are now entering a period when we should be alert to signs of a down turn in economic activity which might call for a relaxation of credit restraint. This is particularly so since, if business and consumers become convinced there is no likelihood of early tax relief, we may see changes in both business plans and consumer anticipations. If such a course were followed - i.e. by keeping on the present restraint and keeping banks under pressure to supply reserves through continuing a high level of borrowings from us - action on the discount rate would depend on the effect of our open market policy. Regardless of whether rates in the short-term market stay where they are, or whether they continue to move up and away from the discount rate it seems to me open market operations represent the first step. In other words, let an increase in the discount rate be an effect of developments in the open market, rather than have the discount rate give a signal which I don't think we are in a position to give as to the longer range outlook."

Mr. Mills wondered whether it might be desirable to present a factual analysis, perhaps in the monthly reviews of the Federal Reserve Banks, which would give some guidance as to the reasons for changes in the interest rate structure. By explaining the normal relationships, Mr. Mills thought that readers would know that the recent increase in long term interest rates was a reflection of changes in supply of and demand for funds, and not a reflection of a deterioration in the quality of public credit.

Mr. Sproul felt that, as had been indicated by Mr. Leach, the only kind of statement that would resolve the uncertainties and clear away the vapor now in the market would be a statement by the Treasury as to what it is planning to do in the way of financing.

Chairman Martin noted that discussions were going on currently at the Treasury regarding its financing problem, particularly the question

of how to deal with maturing Series F and G bonds. He questioned whether anything but action by the Treasury would reduce uncertainty with respect to interest rates on Treasury securities.

Mr. Evans stated that he still questioned whether the policy of restraint followed by the Federal Open Market Committee in recent months had been as restrictive as would have been desirable, that most classes of bank loans were now higher than a few months ago when the Federal Open Market Committee felt the expansion then taking place should be restrained, and that while he did not know whether this was the time to increase the discount rate, he would be in favor of some tightening in the situation generally.

Mr. Sproul said that he did not believe that bank credit could be gotten easily for any purpose at the present time, that loans had not been increasing since the first of this year, and that he would anticipate some seasonal decline in bank loans during the next few weeks.

At this point Mr. Carpenter, Secretary of the Board of Governors, joined the meeting.

Mr. Szymczak said that if there were to be further tightening along the lines suggested by Mr. Evans, the question was whether it should be done by an increase in the discount rate at this time, by taking other action to limit advances made by the Federal Reserve Banks, or whether restriction should be by open market operations. He felt that in any event it would be necessary for the System to supply reserves to the

market for temporary periods to avoid excessive strain.

Mr. Robertson expressed the view that, in the light of the comments made by Mr. Sproul and the views on the economic and credit situation discussed at this meeting, it would seem difficult to justify not "throwing up a red flag" to indicate the dangers in the situation. He suggested that if this were done by an increase in the discount rate and the situation turned out differently, the action could quickly be reversed.

Mr. Rouse said, in response to Chairman Martin's question, that he felt an increase in the discount rate would have quite a noticeable effect in the money market at this time, that such effect would depend upon the amount of the increase, and that if an increase of as much as 1/2 per cent were to be made, the effect would be very marked.

Mr. Sproul inquired as to the purpose of the "red flag" mentioned by Mr. Robertson. He said that he was not particularly worried about the present situation except in the sense that, after the economy has been going along at high levels for a long period, it seemed inevitable that there would be a decline in activity at some time. The present situation appeared to be strong with a danger of some dropping off later on, but at least in terms of prices it did not appear to be inflationary. Mr. Sproul felt that use of open market operations would prove a much more flexible instrument at this stage than would the use of the discount rate. Continued pressure on bank reserves through open market operations would not try to express a judgment of the Federal Reserve on the economic outlook, in the same

way and to the same extent as would an increase in the discount rate, and would be instantly reversible if that seemed called for. He also felt it would not be desirable to try to shock the whole community by taking action on the discount rate when the Treasury was about to go to the market for new money.

In response to a question by Mr. Szymczak, Mr. Rouse stated that the Treasury would find it necessary to make some kind of a statement as to its handling of maturing F and G bonds within the next 10 days.

There followed a general discussion of possible changes in the Treasury balance, in excess reserves of member banks, and in borrowings at the Federal Reserve Banks during the next several weeks, during which it was suggested that by early April borrowings were likely to be somewhere in the neighborhood of 1-3/4 to 2 billion dollars assuming that some further gold outflow took place.

Mr. Youngdahl noted that the Treasury had drawn down its balance to very low levels, that "float" is now very high, and that the present money market may not be a good indicator of short-term interest rates because of the reserves that have been made available from the Treasury balance and float. He felt that in the next two weeks there would be a substantial adjustment in the money market and that the rate on Treasury bills, which is now around 2 per cent, might move back to 2.10 or 2.12 or higher, if banks became less willing to borrow. Mr. Youngdahl suggested that it might be desirable to have some additional pressure against borrowing

in the form of an increase in the costs of discounting.

Chairman Martin said that a persuasive case could be made for increasing the costs of borrowing at the Federal Reserve Banks, that the principal offsetting consideration was that the Treasury would find it necessary to go to the market very shortly. If the Treasury should decide to go the market for long-term funds, the Chairman said, such action would fit in extremely well with credit policy.

Mr. Thomas felt that it might be better to act now to increase restraint on the money market and get the adjustment out of the way before the Treasury came into the market, since otherwise it would be difficult for the Federal Reserve to tighten conditions after the Treasury had made an announcement.

Mr. Sproul said that while the committee would not wish to support a Treasury financing as such through open market operations, he did not think it could ignore the Treasury situation; that we were now in a war-time economy with war-time financing having to be done at a most inappropriate time in terms of the economic situation and credit policy. By use of open market operations, the System could get pressure in the best possible way without having to make a judgment as to future prospects which it was not in a position to forecast with any degree of certainty.

Chairman Martin stated that if a signal such as Mr. Robertson suggested was given by raising the discount rate when it would lead the market, as it would at the present time, it might achieve what was wanted in

the way of restraint; it would, moreover, be a most effective psychological factor indicating the judgment of the central bank as to the economic outlook, quite apart from any judgment that might be indicated on the interest rate structure. With respect to Mr. Sproul's suggestion for letting open market operations determine the additional pressure, the Chairman said he assumed this really meant a lack of open market operations, a lack of supplying additional reserves to the market.

Mr. Sproul stated that he meant to avoid supplying reserves beyond what was needed to offset the effect of foreign transactions and currency demand on the reserve position of the member banks, and then the Federal Reserve should follow up, rather than anticipate, the losses in reserves resulting from a gold outflow or increase in currency. He felt that this general approach should be followed. As to the next few weeks, the course of open market operations would depend on whether the committee wished to permit drains resulting from further gold outflow and currency demand to have their full effect in the money market. It was not a question of putting ease into the market, Mr. Sproul said, but a question whether the System should maintain the re-created pressure that could be expected in a week or ten days, or whether it should take affirmative or negative action to tighten the money market further.

Mr. Mills felt that any further gold outflow and increase in currency demand should be permitted to have their full restraining effects, and Mr. Evans agreed with that view.

During the ensuing discussion, it was suggested that the next meeting of the executive committee would be held in about two weeks when the rebuilding of the Treasury balance and seasonal increases in currency circulation would be having their effects. Under these circumstances, Mr. Mills felt that a decision in the matter should be delayed until that time.

At Chairman Martin's suggestion it was agreed that the next meeting of the executive committee would be held at 10:30 a.m. on Wednesday, April 8, 1953. In the meantime, he stated, it appeared that the market would continue tight and it was his suggestion that operations of the System account be carried on during this period so as not to encourage ease. This suggestion was approved unanimously.

In discussing the general instructions to be issued to the New York Bank, Mr. Rouse suggested that the limitation in the second paragraph regarding purchases of special certificates of indebtedness for the temporary accommodation of the Treasury be reduced from $2 billion to $1 billion.

> 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 to exercising restraint upon inflationary

developments, to correcting a disorderly situation in the Government securities 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 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 $1 billion;

(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 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 at any one time by the Federal Reserve Banks shall not exceed in the aggregate $1 billion.

Mr. Carpenter withdrew from the meeting at this point.

Chairman Martin then referred to a memorandum from Mr. Vest dated March 20, 1953, concerning implementation of actions taken at the meeting of the Federal Open Market Committee on March 4 and 5, 1953, relating primarily to the recommendations contained in the report of the ad hoc subcommittee on the Government securities market. A copy of Mr. Vest's memorandum had been sent to each member of the executive committee before this meeting. There was a brief discussion of the memorandum, during which it was agreed that the matters referred to therein be taken up at the next meeting of the executive committee.

Thereupon the meeting adjourned.

Secretary