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, July 20, 1954, at 10:45 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Robertson
Mr. Bryan, Alternate
Mr. Vardaman, Alternate
Mr. C. S. Young, Alternate

Mr. Mills, Member of the Federal Open Market Committee

Mr. Thurston, Assistant Secretary
Mr. Vest, General Counsel
Mr. Thomas, Economist
Mr. R. A. Young, Associate Economist
Mr. Rouse, Manager, System Open Market Account
Mr. Carpenter, Secretary, Board of Governors
Mr. Sherman, Assistant Secretary, Board of Governors
Mr. Youngdahl, Assistant Director, Division of Research and Statistics, Board of Governors
Mr. Willis, Secretary, Federal Reserve Bank of New York

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meetings of the executive committee of the Federal Open Market Committee held on June 23 and July 7, 1954, were approved.

Before this meeting there had been sent to the members of the committee a report prepared at the Federal Reserve Bank of New York covering open market operations during the period July 7 to July 15, 1954, inclusive, and at this meeting there was distributed a supplementary report covering commitments executed July 16-19, 1954, inclusive. In commenting on the reports, copies of which have been placed in the files of the Federal Open Market Committee, Mr. Rouse noted that the System account's holdings of $167,150,000 of Treasury bills due July 22, 1954 were tendered, subject to allotment, on Monday, July 19, in exchange for the new issue of 91-day bills due October 21, 1954, but that the tender was made at a price below the range of accepted bids. Mr. Rouse stated that dealers were having a difficult time reducing their positions and that at the close of business last night they were holding a little more than $500 million in Treasury bills. He also commented that in managing the System account he had been trying to take advantage of opportunities to dispose of bills during the last few weeks.

Upon motion duly made and seconded, and by unanimous vote, the transactions in the System account during the period July 7-19, 1954, inclusive, were approved, ratified, and confirmed.

Mr. R. A. Young made a statement reviewing recent economic developments substantially in accordance with the summary of economic conditions contained in the staff memorandum dated July 16, 1954, copies of which were distributed before this meeting. Mr. Young noted that economic conditions had shown unusual stability recently, following marked declines in activity and employment from peaks reached a year ago. An important feature of the current situation, Mr. Young said, was that business inventories were still being reduced as production was continuing below the total of final takings by consumers, business, and Government. Such reductions in business inventories might be laying the groundwork for some advance in production later, and Mr. Young suggested that definite signs of recovery in the economy might show up in the not too distant future.

Mr. Young went on to comment on views expressed at the Merrill Center for Economics which he had attended at Southampton, Long Island, during the past three weeks, at which some thirty economists were present for the purpose of discussing the general subject of how instability in the American economy might affect trading in the free world. In this group, there was considerable optimism regarding short-run developments in the economy, it being the consensus that the current recession had gone about as far on the down side as was likely without some new forces of an external nature, and that no such forces which might cause a further downward movement were apparent at present. There was a good deal of reservation, however, as to how strong the forces of growth might be over the coming years and whether the peak of the coming revival in economic activity, if such a revival took place, would be substantially in excess of the high levels reached by the economy during 1953.

Mr. C. S. Young stated, in response to Chairman Martin's inquiry, that Mr. R. A. Young's comments on the economic situation about told the story for the Chicago area. As he had indicated before, Mr. Young said that he had not been as optimistic as many others regarding the economic outlook and that he had been particularly fearful that the building industry would not maintain during the rest of 1954 the rate of activity it had shown earlier this year. There were soft spots in industry in the Chicago District, Mr. Young said, and in his opinion some further readjustment in business inventories would take place. The over-all picture, however, was relatively good.

Mr. Bryan had no serious reservations about the review of the economic situation that had been presented but said that he was puzzled as to what was going to be the source of a long-sustained upward movement in the economy. As to the more immediate outlook, there was real concern in the Atlanta District regarding this year's crops and the Reserve Bank expected to be confronted with problems growing out of run-offs of deposits and related developments at country banks in much of the area. Mr. Bryan also commented on vacancies in store and office buildings in various cities of the district, stating that the commercial component of the building industry might not continue to be as strong a sustaining force to the economy of the Sixth District as it has been heretofore.

In response to a question from Mr. Vardaman, Mr. R. A. Young said that unfilled orders of manufacturers were still declining but that new orders had been rising recently although they were not yet up to the current level of sales. This, he noted, was particularly relevant with respect to the durable goods sector of industry.

At Chairman Martin's request Mr. Thomas commented on capital markets and the credit situation. Loans and investments of reporting member banks had shown about the usual seasonal changes since mid-June. The money supply was increasing when measured in terms of both demand and time deposits and after adjustment for seasonal influences. Reserve positions of banks had been somewhat less easy during the past few weeks than had been anticipated owing principally to a temporary increase in foreign balances at the Reserve Banks. Mr. Thomas also presented a sheet showing an estimated pattern of reserve changes by weeks during the remainder of July and August as well as a tabulation showing estimated weekly averages of free reserves from July 14 through September 1. The latter tabulation indicated that, if all maturing bills in the System account were permitted to run off, free reserves would be in the range of $500-800 million during the remainder of July and August except during the week of August 4 when they would probably exceed $1,100 million.

Mr. Rouse said that the estimates prepared at the Federal Reserve Bank of New York checked closely with those presented by Mr. Thomas.

Chairman Martin stated that on the basis of the economic and credit review and the projections of reserve changes that might be anticipated during the next few weeks, it would appear that the program being carried out by the committee was about right and that developments in the money market were working out pretty well in line with what the committee had hoped for at its preceding meeting. He suggested that the members of the committee first consider whether any change was called for in the general policy being pursued, as it might apply during the next two weeks. None of the members of the committee indicated that a change was called for at this time.

Mr. Rouse stated that in his opinion the atmosphere in the money market had been just about what the committee indicated that it desired at its meeting on July 7.

Chairman Martin expressed the view that the volume of free reserves indicated by the projections presented by Mr. Thomas for the next few weeks would be about right. It was his feeling that a little "topping" would be desirable during the first week of August when payment would be made for the Treasury's offering of $3-1/2 billion of tax anticipation certificates, to be dated August 2, 1954, and to mature March 22, 1955. After that period, Chairman Martin felt that the committee would have to watch the situation carefully in order to prevent the volume of free reserves from getting out of hand.

Mr. Robertson agreed with this statement generally, adding that he would not object to some bulge in free reserves during the week of August 4 although he would be happier if the volume were below the projected figure of $1,120 million.

Mr. Rouse commented that it might be possible to reduce the volume of free reserves during that week by selling from the System account some of the bills that would otherwise mature during the weeks of August 11 and 18, with the result that the run-off in System holdings of bills during those two weeks would be smaller than projected.

Chairman Martin suggested that the next meeting of the executive committee be held on Tuesday, August 3, 1954, at 10:45 a.m. which would provide an opportunity to review the situation at about the time the

Treasury's cash offering of tax anticipation bills had been completed, and there was agreement with this suggestion.

Mr. C. S. Young stated that he would like to see the System account take advantage of any opportunity to sell bills it was holding, in addition to run-offs of bills maturing during the next few weeks, as a means of reducing the System's portfolio.

Mr. Bryan said that he felt the entire policy and operation of the Federal Reserve System had been brilliant throughout the recent period, although, as stated at the meeting of the full Committee on June 23, 1954, he had some reservation as to whether there was not too much emphasis being placed on the volume of free reserves. He had grave doubts whether the rediscount rate should be left at its present level of 1-1/2 per cent in the light of open market and reserve-requirement policies that have produced open market rates well below that figure. Mr. Bryan said that he would be much happier if the discount rate and the tradition of the American banking system were such as would cause the banking system to obtain a portion of its reserves by a much higher level of discounts and advances at the Reserve Banks than is now indicated. Despite these reservations, Mr. Bryan emphasized that he felt the System had handled monetary policy and operations brilliantly in the recent past.

Mr. Mills reverted to the question whether it would be desirable to sell bills from the System account during the first week of August, stating that this would be the week in which the Treasury would receive payment for the $3-1/2 billion of tax anticipation certificates to be issued. His concern was that the distribution of reserves among central reserve city, reserve city, and country banks might not be satisfactory and that while, in the aggregate, there might be a large volume of free reserves, these might be concentrated for a period at country banks while there might be a paucity of free reserves at reserve city and, particularly, at central reserve city banks. It was Mr. Mills' thought that it might be desirable to allow a greater latitude in free reserves during the period than was contemplated under the suggestion for selling bills during that week.

Mr. Rouse indicated that he agreed with the views expressed by Mr. Mills.

Chairman Martin felt this was a pertinent comment and that the situation should be watched closely. It was his view that, as he had indicated earlier in the meeting, some excess of reserves during the period of the Treasury financing was not going to be harmful.

None of the members of the committee disagreed with this view, and it was understood that operations for the System account would be continued in terms of the program authorized at the preceding meeting of the executive committee and in the light of the discussion at this meeting.

Mr. Robertson referred to a memorandum which, pursuant to the suggestion made at the meeting of the executive committee on June 8, 1954, had been prepared in the Securities Department of the Federal Reserve

Bank of New York under date of July 6, 1954 relating to transactions for cash delivery for the System open market account. Mr. Robertson said that on the basis of the pros and cons set forth in this memorandum, copies of which were distributed at the meeting on July 7, 1954, it would appear that there were situations where cash trading, as contrasted with the practice of limiting transactions to "regular" (next day) delivery, would make it possible to do a better job of executing open market policy. It was his suggestion, therefore, that the existing practice be modified and that the executive committee authorize the Manager of the System Open Market Account to trade in Treasury bills on both a cash and regular delivery basis, depending on market circumstances. It was Mr. Robertson's opinion that it would be desirable for the Federal Reserve Bank of New York to engage in some cash trading in the weeks immediately ahead, if market circumstances permitted, in order to develop System experience with such transactions. He noted that the memorandum prepared at the New York Bank on the subject indicated there might be certain operating difficulties with cash trading, and he felt that it would be helpful to take the measure of these problems through actual experience and to give those operating the System account an opportunity to solve the difficulties when not under pressure. Mr. Robertson also suggested that if the authorization which he proposed were given to the Manager of the System Account, dealers be notified that the account was willing to engage in cash transactions in Treasury bills under appropriate circumstances without, of course, any implication that the System wished to encourage cash trading by others.

Chairman Martin inquired of Mr. Vest whether this suggestion involved problems in terms of the authorization given by the full Committee to the executive committee.

Mr. Vest stated that, while he understood that transactions for the System account had almost always been on a "regular" delivery basis and while this customary practice had been a matter of comment at a meeting of the full Committee some years ago, it was his opinion that the directive of the Federal Open Market Committee under which the executive committee was now operating was phrased in such broad language as to permit a change in operating technique of the sort proposed by Mr. Robertson. Mr. Vest read portions of the full Committee's directive, noting particularly that part which authorized the executive committee to arrange for transactions with a view, among other things, "to the practical administration of the account." He felt that this clause was sufficiently broad to cover authority for a change such as Mr. Robertson proposed. At the same time, it was Mr. Vest's view that it might be desirable to bring to the attention of the members of the full Committee the change in practice that would be involved in Mr. Robertson's suggestion.

Chairman Martin stated that his understanding of the proposal was that there would be an authorization to the Manager of the System Account to engage in cash transactions as distinguished from regular delivery transactions in the event it seemed desirable to do so.

Mr. Robertson stated that this was correct but that he would hope that some transactions on a cash delivery basis would be executed during the next several weeks so as to provide some experience in effecting transactions in that manner.

Mr. Rouse said that he saw no objection to the proposal and, in fact, he felt it might be useful to have the authority. Mr. Rouse also suggested that it would be desirable to furnish all members of the full Committee with a copy of the memorandum of July 6 prepared at the Federal Reserve Bank of New York to which Mr. Robertson had referred, and it was understood that this procedure would be followed.

Thereupon, upon motion duly made and seconded, Mr. Robertson's suggestion as set forth above was approved unanimously.

Mr. Rouse suggested that the existing limitation of $750 million in the first paragraph of the directive to be issued to the Federal Reserve Bank of New York be continued in view of the possibility of large transactions for the System account during the next two weeks.

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 (a) to relating the supply of funds in the market to the needs of commerce and business, (b) to promoting growth and stability in the economy

by actively maintaining a condition of ease in the money market, and (c) 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 $750 million;

(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 $500 million;

(3) To sell direct to the Treasury from the System account for gold certificates such amounts of Treasury securities maturing within one year as may be necessary from time to time for the accommodation of the Treasury; provided that the total amount of such securities so sold shall not exceed in the aggregate $500 million face amount, and such sales shall be made as nearly as may be practicable at the prices currently quoted in the open market.

Thereupon the meeting adjourned.

Winfield Thurston

Assistant Secretary