

FORTIETH

# ANNUAL REPORT

*of the*

BOARD OF GOVERNORS OF THE  
FEDERAL RESERVE SYSTEM



COVERING OPERATIONS FOR  
THE YEAR

1953

bills, and that if there were to be any change from this position, such a change should be determined upon by a meeting of the entire Federal Open Market Committee, not by the executive committee. It was also the view of those voting for this motion that to assist in the development of depth, breadth, and resiliency in the Government securities market, the practice which had been followed for some months of refraining from purchases of certain Treasury securities during periods of Treasury financing was desirable. It was noted that the adoption of this practice had not been reflected in an unfavorable experience on the part of the Treasury in its refunding operations.

In adopting the policies stated, which were to be followed until such time as they might be superseded or modified by further action of the Federal Open Market Committee, it was made clear that the Committee could change these policies at any time it might wish to do so in the future in the same way that it could change any other policy which it had adopted; and it was noted that a meeting of the Federal Open Market Committee could be convened on 24 hours' notice if necessary for the purpose of considering a change in these or other policies.

The members of the Committee who opposed adoption of the policies embodied in this action expressed substantially the views that had been stated in favor of the action taken at the June meeting in rescinding similar policies that had been adopted in March. There was a concern that the Committee was trying to write into a "constitution" of the Open Market Committee a prohibition against actions deemed undesirable by the Committee at a particular time; that the resolution put into the form of a continuing directive a matter which should be considered, in the light of existing conditions, at each meeting of the Committee and its executive committee. They felt it preferable for the executive committee of the Federal Open Market Committee to be free to use its judgment, within the limits of the Committee's general credit policy at the time, as to the best method of achieving the objectives of credit policy, in whatever circumstances might arise between meetings of the full Committee.

DECEMBER 15, 1953

#### 1. Authority to Effect Transactions in System Account.

The following directive to the executive committee was approved:

The executive committee is directed, until otherwise directed by the Federal Open Market Committee, to arrange for such transactions for the System open market account, either in the open market or directly with the Treasury (including purchases, sales, exchanges, replacement of maturing securities, and letting maturities run off without replacement), 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, (c) to correcting a disorderly situation in the Government securities market, and (d) to the practical administration of the account; provided that the aggregate amount of securities held in the System account (including commitments for the purchase or sale of securities for the account) at the close of this date, other than special short-term certificates of indebtedness purchased from time to time for the temporary accommodation of the Treasury, shall not be increased or decreased by more than 2 billion dollars.

The executive committee is further directed, until otherwise directed by the Federal Open Market Committee, to arrange for the purchase direct from the Treasury for the account of the Federal Reserve Bank of New York (which Bank shall have discretion, in cases where it seems desirable, to issue participations to one or more Federal Reserve Banks) of 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 2 billion dollars.

Votes for this action: Messrs. Martin, Chairman, Sproul, Vice Chairman, Erickson, Evans, Fulton, Johns, Mills, Powell, Robertson, and Szymczak. Votes against this action: none.

This directive was changed to provide, as the central objective of current credit policy, that transactions for the System open market account should be with a view "to promoting growth and stability in the economy by actively maintaining a condition of ease in the money market." The corresponding clause of the directive issued by the Committee at its meeting on September 24, 1953, provided that transactions be with a view "to avoiding deflationary tendencies"; at the June 1953 meeting, the instruction read, "to avoiding deflationary tendencies without encouraging a renewal of inflationary developments (which in the near future will require aggressive supplying of reserves to the market)"; and in March 1953, the Committee had directed, in this respect, that transactions be with a view "to exercising restraint upon inflationary developments."

These clauses in the directives issued by the Federal Open Market Committee at its meetings in 1953 indicate the adjustments made in credit policy to adapt it to the unfolding economic situation. The opening months of the year were characterized by a very high level of economic activity, a strong demand for credit, continued growth in the money supply (seasonally adjusted), and, despite fairly stable commodity prices, more reason for con-

cern about the possibility of inflationary developments than of deflationary movements. By June, the situation had shifted to one of less concern with inflationary developments and, instead, growing uneasiness in many areas regarding the future, even though actual production, employment, and incomes remained at or close to record levels, total credit demands were large, and commodity prices were relatively stable. When the Committee met toward the end of September, some downward adjustments had begun to appear in the economy and a more active policy of supplying reserves was adopted. This policy did not make specific provision for avoiding inflationary tendencies since they did not appear likely to threaten.

In the period since September, the decline in economic conditions, though moderate, had been unmistakable. Although wholesale prices had been steady, unemployment at a low level in the period as a whole, and nonfarm income not much below the peaks reached in the summer of 1953, declines had been experienced in industrial production, factory employment, gross national product, and farm income. In the over-all view, the decline constituted the first significant interruption of economic expansion since 1949. Inventory accumulation had been a subject of some concern early in the year, but in the third quarter the rate of accumulation dropped and in October inventories were reduced somewhat. Bank credit and the money supply had shown much less than the usual seasonal increases, even though banks had utilized additional reserves made available to them to purchase Government securities in the absence of loan demand.

Studies of prospects for the months immediately ahead indicated the probability that, after the holiday and other year-end drains, reserve funds would be supplied in January by the post-holiday return flow of currency, and that in subsequent weeks the usual seasonal contraction in private credit demands, offset only in part by a rebuilding of Treasury balances, would tend toward the maintenance of relatively easy money markets into the second quarter of the year. Under the circumstances some reduction in the System's portfolio, following a temporary increase to meet large December needs, was to be expected. Nevertheless, it was the view of the Committee that System policy should in no sense be one of restraint during the period immediately ahead, and it was in this setting that it approved a continuation of the general policy pursued in recent months of supplying or maintaining reserves adequate to promote growth and stability in the economy with, however, the understanding that in carrying out operations for the System account there would be more emphasis on a program of actively maintaining a condition of ease in the money market.

At this meeting, reference also was made to the action taken by the Committee on September 24, 1953 in approving a motion that "the Federal Open Market Committee take the position that operations for the System account in the open market be confined to short-term securities (except in the correction of disorderly markets) and that during a period of Treasury financing

there be no purchases of (1) maturing issues for which an exchange is being offered, (2) when-issued securities, or (3) outstanding issues of comparable maturity to those being offered for exchange; and that these policies be followed until such time as they may be superseded or modified by further action of the Federal Open Market Committee."

Mr. Sproul moved that the last clause of the foregoing action taken at the meeting on September 24, 1953 be amended to read, "and that these policies be followed until the next meeting of the Federal Open Market Committee."

Mr. Sproul's motion was put by the Chair and lost.

Votes against the motion: Messrs. Martin, Chairman, Evans, Fulton, Johns, Mills, Powell, Robertson, Szymczak, and Vardaman. Votes for the motion: Messrs. Sproul, Vice Chairman, and Erickson.

In proposing this motion, Mr. Sproul stated that he was in no way altering his opposition to the general purport of the action approved by the Committee on September 24 but that he felt the proposed language would correctly reflect the sense of that meeting, that is, that the action would be subject to review at the next meeting of the Committee.

Those opposed to the motion felt that, while they would not necessarily have any objection to considering the question at the next or any other meeting of the Committee, they would prefer not to have the proposed change adopted inasmuch as it would mean that the action taken at the meeting on September 24 would automatically become ineffective after the next meeting of the Committee unless positive action were taken to renew it.

## 2. Transactions for the Purpose of Altering the Maturity Distribution of Securities in the System Open Market Account.

Mr. Robertson moved that the Federal Open Market Committee adopt the following policy to be followed until such time as it may be superseded or modified by future action of the Committee:

Transactions for the System account in the open market shall be entered into solely for the purpose of providing or absorbing reserves (except in the correction of disorderly markets), and shall not include offsetting purchases and sales of securities for the purpose of altering the maturity pattern of the System's portfolio.

After discussion, Mr. Sproul, without accepting in any way the idea of a perpetual policy such as was suggested by Mr. Robertson's motion, moved that that motion be amended to provide that it would be effective until the next meeting of the Federal Open Market Committee.

Mr. Sproul's motion was put by the Chair and lost.

Votes against Mr. Sproul's motion: Messrs. Martin, Chairman, Evans, Fulton, Johns, Mills, Powell, Robertson, Szymczak, and Vardaman. Votes for the motion: Messrs. Sproul, Vice Chairman, and Erickson.

Mr. Robertson's motion was then put by the Chair and carried.

Votes for Mr. Robertson's motion: Messrs. Martin, Chairman, Evans, Fulton, Johns, Mills, Powell, Robertson, Szymczak, and Vardaman. Votes against the motion: Messrs. Sproul, Vice Chairman, and Erickson.

This action was taken in the light of an authorization by the executive committee of the Federal Open Market Committee at its meeting on November 23, 1953 under which the Manager of the System Account made certain purchase and sale transactions in the short-term sector of the Government securities market in the amount of 70 million dollars. The full Committee had not previously specifically considered the question whether such transactions might be entered into during periods other than at a time of Treasury financing. The purpose of such "swap" transactions (under which securities having a maturity of 12½ months or less were sold from the System account and replaced with a like amount of Treasury bills maturing in January 1954) was to increase the proportion of the System account in the form of Treasury bills of shortest maturity, a move which the executive committee then felt to be desirable as a means of facilitating prospective operations in carrying out credit policy after the turn of the year.

The votes for Mr. Robertson's motion were on the basis that, generally speaking, "swap" transactions were not desirable in terms of the general policy approved at the meeting on March 4-5, 1953 of not now supporting any pattern of prices and yields in the Government securities market and of intervening in that market solely to effectuate the objectives of monetary and credit policy (including correction of disorderly markets). It was felt that if the System open market account were to engage in purchases and sales in the open market without altering total holdings of securities in the portfolio, the objective of such transactions would not be clearly discernible to the market and thus might cause confusion and uncertainty as to credit policy and, in so doing, militate against the depth, breadth, and resiliency sought in the Government securities market. It was understood, however, that the Committee should have no hesitancy in reversing this action in the event circumstances arose which made that seem to be desirable, and Mr. Sproul's motion was opposed for that reason.

Those opposed to this action took the position that, while supplying reserve funds to the market or taking them out was the primary function of open

market operations, to say that it was the sole function would be much too narrow an interpretation; much narrower than saying that the sole purpose was to effectuate the objectives of monetary and credit policy. They felt that "swaps" for the System account which had taken place recently were an appropriate use of the System portfolio, that they had helped the banks and the whole market to readjust their short maturities as they desired and had increased the System's holdings of bills maturing in January 1954 which might be useful in carrying out credit policy. It was their view that "swaps" in the account need not interfere with market flexibility, but might in fact assist the market in adjusting to the needs of investors, and that there was no compelling reason to proscribe them.