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Chairman Eccles | Statement of views of
Allan Sproul | Allan Sproul, edited by Robert Rouse.

The reasons advanced, heretofore, suggesting the desirability of an increase in rates on Treasury certificates of indebtedness and of introducing some flexibility into the short-term rate structure, became more compelling in the face of the refunding problem facing the Treasury during the fiscal year, 1947-48. Present estimates indicate that during the first six months of the fiscal year, surplus cash will not permit substantial debt retirement other than the unexchanged portion of maturing debt. Meanwhile, the tendency of banks to reach for longer-term securities, and the downward pressure on long-term interest rates, which are the inevitable consequences of maintaining the wartime pattern of short-term rates, continues. The former is obscured in the figures by changes in maturities with the passage of time, but it is apparent in market transaction. (Based on the increase of over 350 million dollars in holdings of Treasury bonds by reporting banks in 101 cities since April 9, 1947, it is estimated that holdings of Treasury bonds by all banks increased between 500 million and 600 million dollars during that period.) The latter, that is, the downward pressure on long-term interest rates, has been obscured by Treasury sales, but the sale of more than 750 million dollars 2 1/2 per cent restricted issues and 170 million bank eligible issues since April 10 served to move prices down only 1/2 to one point for the restricted issues and less for the bank eligible issues. The action of the market indicates that this loss would be quickly recovered if sales diminish or cease.

Because the Treasury will have to refund a substantial amount of notes and bonds during the fiscal year now beginning, it is faced with the necessity of deciding whether to perpetuate this undesirable situation, with its encouragement to debt monetization, for a further extended period. A refunding issue of notes or intermediate bonds priced on the present rate pattern would freeze that pattern into the rate structure for another term of years, probably express itself through an excess and unwanted premium on the new issues. Similar refunding issues priced on the present market which, in terms of yield is below the rate pattern, would actually impose a reduction in that pattern. Refunding of maturing notes and bonds with certificates, at present rates, would intensify existing undesirable pressures. It seems to me almost imperative, therefore, to narrow the spread between short-and long-term rates and to introduce some flexibility and uncertainty into the rate structure if the refunding program is to be geared to a sound policy of debt management and credit policy. The way to proceed, it seems to me, is immediately to adopt a program which will consolidate outstanding issues of certificates into four or six issues, with a gradual increase in the rate. With such a program, refunding into certificates should be possible, at least until a better rate structure has developed.