

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

July 21, 1943

Chairman Eccles

System Account transactions in
certificates

L. M. Piser

CONFIDENTIAL

As Mr. Rouse pointed out in the meeting yesterday, the System's relation to the certificate market can be divided into two periods. To the end of January, the certificate market required a substantial amount of support. The System's holdings at the end of January reached a peak of 1.1 billion dollars. Since then, the market for the most part has been able to take care of itself, and the System on balance has sold certificates.

As is shown by the attached table, 9- to 12-month certificates were purchased in the period from July 29 to October 28 at an average yield of 0.76 per cent, compared with your suggested average of 0.875 per cent. In the next 3-month period, 9- to 12-month certificates were purchased at an average yield of 0.78 per cent. In the 3 months from February 3 to April 28, there was a large demand in the market, and the System sold 9- to 12-month certificates at an average yield of 0.78 per cent. In the last 3 months, the longest certificates have been sold at an average yield of 0.77 per cent.

In the 3 months from October 28 to February 3, 6- to 9-month certificates were purchased at an average yield of 0.68 per cent, and in the following 3 months the same yield was continued on certificates of similar maturity. In the last 3 months, the yield on purchases of these issues has been 0.75 per cent, which is your suggested yield.

From February 3 to April 28 3- to 6-month certificates were purchased at an average yield of 0.55 per cent, and in the last 3 months such purchases have been made at 0.71 per cent, compared with your suggested figure of 0.625 per cent. In the last 3 months, purchases of certificates maturing within 3 months have been made at an average yield of 0.47 per cent, compared with your suggestion of 0.50 per cent.

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The yields on purchases have been far out of line, particularly in recent months, with the yields that you suggested. The policy followed by Mr. Rouse has had two aspects, which it seems to me should be continued. First, he has recently purchased 3-month certificates at yields somewhat above the buying rate; the point at which he has supported longer certificates

has been considerably higher, with the line of yields on longer certificates practically level. The purpose of this procedure is to reduce the amount of return that can be made from playing the pattern of rates on certificates in the first few months after issuance, where the most unreasonable return would be made if the System followed a rigid pattern.

Second, he has allowed the certificate market to fluctuate fairly widely and has made purchases only when a large supply of certificates could not be placed. With yields on certificates fluctuating over a considerable range, the holder has no assurance that certificates can be sold at a particular yield at any particular time. The purpose of this policy is again to discourage playing of the pattern of rates on certificates. It seems to me that both of these policies have considerable merit and should probably be continued.

The only criticism that I have to offer is that perhaps new issues of certificates should not be purchased at yields quite so low as they have been purchased in the past and that if yields tend to decline immediately after the issuance of new certificates the System should sell more aggressively from its holdings. I think that the maintenance of a rigid pattern would tend to increase playing of the pattern of rates. It seems to me preferable to allow the market considerable latitude in which to fluctuate and to try to keep the maturities of longer than 3 months on as nearly a horizontal line as possible.

SYSTEM ACCOUNT TRANSACTIONS IN CERTIFICATES

Issue	July 29 - Oct. 28		Oct. 28 - Feb. 3		Feb. 3 - Apr. 28		Apr. 28 - July 14	
	Amount ^{1/}	Average yield	Amount ^{1/}	Average yield	Amount ^{1/}	Average yield	Amount ^{1/}	Average yield
Purchases								
Aug. 1	84,390	.76	124,610	.68	64,400	.55	16,000	.47
Nov. 1	--	--	164,044	.78	86,500	.68	12,050	.71
Dec. 1	--	--	--	--	70,600	.73	79,500	.75
Feb. 1	--	--	--	--	--	--	20,000	.75
Apr. 1	--	--	--	--	--	--	51,500	.77
May 1	--	--	--	--	--	--	--	--
Sales								
Aug. 1	--	--	--	--	6,350	.56	--	--
Nov. 1	--	--	--	--	41,300	.68	--	--
Dec. 1	--	--	--	--	31,400	.74	--	--
Feb. 1	--	--	--	--	51,940	.78	--	--
Apr. 1	--	--	--	--	--	--	--	--
May 1	--	--	--	--	--	--	89,200	.77

^{1/} In thousands of dollars.

Note: Purchases on allotment as follows:

Nov. 1 -- \$158,156,000
 Feb. 1 -- 51,940,000
 May 1 -- 296,800,000