B/D 4/21/55
AS

1. Don't want to try to second-guess what you did last week. Shared your doubts about an increase now, in terms of the business situation, but Treasury financing is also a part of the whole economic situation. Think you had a ~~fifty-fifty~~ hard choice, ~~and~~ but the lack of adverse business and market repercussions indicates that you did the right thing in terms of the whole economic situation. Business situation strong enough to take it; Treasury situation needed it.

2. Demonstration of the fact that discount policy is still subordinate to open market policy, and that credit policy as a whole is still frequently the prisoner of the Treasury's financing needs.

3. Open market policy brought about the change in the cost and availability of credit which moved short term market rates of interest up to and above the discount rate. To maintain consistency in use of the various means of credit administration, an increase in the discount rate would soon have become necessary, in any case, unless there was a change for the worse in the ~~economic~~ business situation ~~and in~~ or in the direction of ease in open market ~~policy~~ operations or both.

4. The timing of the change was forced by the Treasury's needs. With the economy again operating at a high level, and with the tax take also high, the Treasury should not have to be coming to the market for new money. But the requirements of the defense program and the peculiar time incidence of tax payments during the fiscal year, will make the Treasury a heavy borrower of new money during the next few months. Private demands for funds are consuming private savings, and the Treasury will have to rely, in considerable part, on the commercial banks for the success of its financing. Market knowledge of this situation, and market expectations that an increase in rate would soon be forced by the combination of private and Treasury demands for credit, in the face of the existing reserve position, made it almost essential to have the

increase out of the way before the Treasury prices its new money borrowing at the end of this month.

5. The implications of this situation are disturbing. Despite our break for freedom, monetary policy has to recognize the continuing need for coordination with Treasury financing, which at times such as this makes it difficult to have a ~~wholly consistent~~ monetary policy geared solely to the business situation. If the Federal finances are out of whack with the ~~economic situation,~~ private economy we can't ignore either one.

6. It is also disturbing to have what seems to be random action by other Federal Reserve Banks, or action at such banks prompted by members of the Board of Governors, forcing the hand of this bank which is situated in the principal money market of the country. If it were not for special Treasury needs as in this instance, however, I think it would be possible for this bank to preserve more independence, although consistency with open market policy would still be necessary. Our views would influence the Board of Governors and other banks as indeed they did in this case postponing an action which otherwise would have been taken earlier when even less justified in terms of the business situation. And, at times, and for a period of time, I think we could have a different and effective rate, even though the emergence of a national market in Government securities, and the increased fluidity of funds, are powerful forces in the direction of uniform rates at the various Federal Reserve Banks.

7. No change.