A meeting of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System in Washington on Monday, December 11, 1944, at 10:10 a.m.

PRESENT: Mr. Eccles, Chairman
Mr. Sproul, Vice Chairman
Mr. Szymczak
Mr. McKee
Mr. Ransom
Mr. Draper
Mr. Evans
Mr. Leach
Mr. Young
Mr. Davis
Mr. Peyton

Mr. Morrill, Secretary
Mr. Carpenter, Assistant Secretary
Mr. Goldenweiser, Economist
Messrs. John H. Williams, Kincaid, and Langum, Associate Economists
Mr. Wyatt, General Counsel
Mr. Rouse, Manager of the System Open Market Account
Mr. Thurston, Special Assistant to the Chairman of the Board of Governors
Messrs. Piser and Kennedy, Chief and Assistant Chief, respectively, of the Government Securities Section, Division of Research and Statistics of the Board of Governors

Messrs. Alfred H. Williams and Gilbert, alternate members of the Federal Open Market Committee

Messrs. Flanders, McLarin, and Day, Presidents of the Federal Reserve Banks of Boston, Atlanta, and San Francisco, respectively

Mr. Koppang, First Vice President of the Federal Reserve Bank of Kansas City

Effective September 15, 1944, Mr. M. J. Fleming resigned as an alternate member of the Committee and Mr. R. M. Gidney, President of the Federal Reserve Bank of Cleveland, was subsequently elected to succeed Mr. Fleming as an alternate member of the Committee for the remainder of the year ending February 28, 1945. Mr. Morrill said that Mr. Gidney had taken the required oath of office.

Before this meeting each member of the Committee received a copy of a report submitted by the examiner in charge for the Board of Governors, covering an examination of the System open market account as of September 9, 1944, made as a part of the regular examination of the Federal Reserve Bank of New York. The report contained no criticisms or recommendations.

> Upon motion duly made and seconded, and by unanimous vote, the report was received and ordered filed.
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> Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the Federal Open Market Committee, held on September 21-22, 1944, were approved.
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> Upon motion duly made and seconded, and by unanimous vote, the actions of the executive committee of the Federal Open Market Committee, as set forth in the minutes of the meeting of the executive committee on September 21, 1944, were approved, ratified and confirmed.

Mr. Rouse distributed copies of a report prepared at the Federal Reserve Bank of New York of open market operations during the period from September 22 to December 6, 1944, inclusive. He also presented a supplementary report covering operations in the account on December 7, 8, and

9, and reviewed briefly, for the information of the members of the Committee, the highlights of the two reports. Copies of the reports have been placed in the files of the Federal Open Market Committee.

> Upon motion duly made and seconded, and by unanimous vote, the transactions in the System account, during the period September 21 to December 9, 1944, inclusive, were approved, ratified and confirmed.

At Chairman Eccles' suggestion there was then read a memorandum prepared by Mr. Piser, under date of December 7, 1944, relating to recommendations made by the executive committee to the Treasury since the last meeting of the full Committee on Treasury bills and the Sixth War Loan Drive and Treasury actions with respect to these matters. The memorandum stated that, of the nine suggestions made, the Treasury had adopted the three which proposed (1) that the Treasury provide a more specific yardstick for subscriptions from brokers and dealers; (2) that the Treasury make no increase in outstanding bills during the drive; and, (3) that the Treasury, in the announcement of the terms of the Sixth War Loan Drive, request the banks not to make loans for the purpose of acquiring drive securities for their own account and that a letter be sent to all commercial banks requesting them to police subscriptions.

Mr. Kennedy made a report of the progress of the Sixth War Loan Drive, stating that the drive already had exceeded the over-all goal of $14,000,000,000 by approximately $500,000,000; that the total subscriptions for the drive probably would reach approximately $19,000,000,000, exclusive of approximately $1,000,000,000 of subscriptions made by banks under the formula for the investment of time deposits and $800,000,000 from Government agencies and trust funds; and that the total subscriptions would be approximately $21,000,000,000 or almost as large as total subscriptions for the Fifth Drive when the goal was $16,000,000,000. He also stated that sales to individuals at the present time amounted to approximately $3,000,000,000, and that it was thought that the quota for sales to individuals would be reached, although the sales of E bonds were lagging. He went on to say that "free riding" during the drive had not been as great as in the Fifth Drive but that pressure for purchases for the purpose of reaching quotas would be greater during the remainder of the Drive and it was during this period that the test would come. Copies of a more detailed report, prepared by Mr. Kennedy under date of December 9, 1944, were distributed during the meeting.

During a discussion of developments during the Sixth War Loan Drive and steps that might be taken in future drives to curb "speculative" and indirect bank purchases of securities, there was agreement with the suggestion that experience during the current drive should be studied carefully so that at the next meeting of the full Committee recommendations with respect to the next drive could be formulated for submission to the Treasury.

There was then read a memorandum prepared at Chairman Eccles' suggestion by Mr. Piser under date of December 8, 1944, relating to the reserve position of banks since the close of the Fifth War Loan Drive and what the estimated reserve needs of the banks would be during the period between the close of the current drive and April of next year. The memorandum pointed out that during the period July 12, to November 15, 1944, when the reserve needs of member banks increased $3,900,000,000, the banks sold to the Reserve Banks $2,900,000,000 of bills and $600,000,000 of certificates and notes, although they purchased from the Federal Reserve Banks approximately $300,000,000 of Treasury notes and bonds. The memorandum also stated that it was estimated that between December 20, 1944, and April 18, 1945, the reserve needs of member banks would be between $2,400,000,000 and $3,000,000,000 and that the increase in the Federal Reserve holdings of Government securities for the purpose of supplying reserves would increase between $1,600,000,000 and $2,200,000,000.

Chairman Eccles commented that the situation as outlined in the memorandum presented the possibility of a significant development between the Sixth and Seventh Drives in that the banks would be likely to sell even larger amounts of certificates during the period for the purpose of building their reserves, which would present the question what the policy of the Committee would be with respect to future purchases of certificates. It was a question, he stated, whether the

System would attempt to lower the yields on Treasury certificates and permit the market to demand a larger premium or whether the yields on certificates should be stabilized at 3/4 of 1 per cent and the yield on 8-10 year bonds should decline to a point where the rate on the latter would be 1-3/4 per cent. He also said that this involved a matter which had been raised by Mr. Rouse as to the instructions to be issued by the executive committee to the Federal Reserve Bank of New York with respect to the purchase of certificates for the System account and which would be considered in connection with the general question of Treasury financing policy, the next subject on the agenda.

At Chairman Eccles' request, there was then read a memorandum which had been prepared at his request and which he stated was in the nature of a supplement to the memoranda presented by him at the last meeting of the Federal Open Market Committee on the subjects of Treasury financing policies and earnings of commercial banks. The memorandum stated that, after giving further consideration to the declining demand for Treasury bills, the continuing difficulties with maintaining a structure of yields on certificates, and the increasing earnings of commercial banks, the following proposals were made, with the suggestion that the Treasury announce the first, third, and fourth proposals shortly after the first of the year:

(1) That the maturity of Treasury bills be extended to four, five, or six months and the rate increased to 1/2 per cent;

(2) That such part of Federal Reserve holdings of bills as will not be needed for future sale in the market be refunded by the Treasury into special issues yielding 1/4 per cent;

(3) That the coupon rate on future issues of certificates be 3/4 instead of 7/8 per cent; and,

(4) That the Treasury issue no additional 2 per cent bonds available for purchase by commercial banks.

Chairman Eccles stated that, while he would not recommend the adoption of these proposals without further study, he did feel that some adjustment in short-term rates was necessary to bring these rates in closer relationship to the existing short-term market situation, and that such a program would be one means of meeting the problem of bank earnings which was a question that was certain to come before Congress sooner or later. He also said that if such a program were adopted the System would be in a much better position to go before Congress, as it would have to do some time next year, to ask for a reduction in the reserves required to be maintained by the Federal Reserve Banks against Federal Reserve notes and deposits and for an extension of the authority to pledge Government securities as collateral for Federal Reserve notes, and that it would also make it unnecessary to raise the question of a revival of the franchise tax on Federal Reserve Bank earnings and the questions that might be associated therewith. He added that the attorneys for the Committee had studied the suggestion that bills in the System account might be refunded by the Treasury through special issues of bills yielding 1/4 per cent and were of the opinion that such a transaction would be an exchange and, therefore, not subject to the $5,000,000,000 limitation on direct purchases of Government securities from the Treasury.

In connection with this point, Chairman Eccles referred to his recent conversation with Under Secretary of the Treasury Bell, relating to the question whether, in connection with the renewal of the Second War Powers Act, an amendment should be suggested that would remove the limitation on the authority of the Federal Reserve Banks to purchase Government securities directly from the Treasury and stated, that although it was felt that the limitation should be removed, it was decided that an amendment should not be suggested at this time as it might endanger the desired extension of the Act as a whole at this session of Congress.

During a discussion of alternative courses that might be pursued, Mr. Sproul stated that the proposals outlined in Chairman Eccles' memorandum raised a number of important questions which should be given more study than had been possible in the short time that the memorandum had been available, and that while he did not have any final opinion on the proposals at this time he did see some possible objections to them. He felt that, while the reduction in rates might moderate the problem of maintaining the pattern of rates, it would not go any considerable distance in eliminating it as it would continue to exist as long as there was any substantial spread between short and long-term rates and the System continued to maintain the pattern. He questioned whether the change would reestablish Treasury bills as a market instrument, as in his opinion the time for accomplishing that had passed and the banks were using certificates and even long-term issues or were borrowing from the Federal Reserve Banks to adjust their reserve positions. He was not convinced that it would be wise to change the pattern of wartime financing in the absence of urgent reasons or reasonable certainty of improvement, because we have been successful in financing a war of unprecedented cost at relatively low and stable rates of interest, and because the System should be very careful to do nothing which might destroy the confidence of the people in our wartime financing methods. To do so, he said, could result in such concern about our currency and bank deposits as to create the inflationary conditions that the country had been able to avoid thus far. He felt that if the System and the Treasury could agree that the area between the 3/8 per cent bill and the 7/8 per cent certificate is outside the agreed pattern of rates, there would be a better basis for maintaining the existing pattern. Furthermore, he stated, if there could be an announcement at the beginning of each war loan drive of an offering of securities to the banks at the end of the drive and if nonbank quotas could be based on what actually could be sold to and held by nonbank investors, the pressure would be taken off nonbank holders of securities to sell in order to buy new issues in each succeeding drive, and this in turn would take some of the buying pressure out of the market. In so far as earnings of the Federal Reserve Banks are concerned, he thought the System might be in a better position if it made some contribution to the Treasury through a restoration of the franchise tax, rather than to become a sort of pensioner of the Treasury through taking securities at less than the market rate. The related matter of private bank earnings, he agreed, showed indications of becoming a serious problem but he preferred, for the immediate present, to permit the banks to see what could be done with their greater earnings for labor, the consumer, and the stockholder, rather than to try to devise a means of taking away the earnings. In other words, he suggested that the banks should consider increasing salaries of employees; increasing the rates of interest paid on time deposits and reducing interest rates on loans; and adding to capital funds from earnings or paying increased dividends, thus enabling the banks to sell additional stock, so that if an opportunity for increased bank lending should develop the banks would be in a position to take the additional risks involved in such loans.

Chairman Eccles stated that the Treasury was considering the problems raised in his memorandum and, therefore, he would like to submit to the Treasury fairly soon a statement which, if an agreement could not be reached by the members of the Federal Open Market Committee as to a recommendation, would be accompanied by the views of the individual members of the Committee.

Mr. Sproul suggested that before a formal statement of Committee views was sent to the Treasury it would be better to have an informal discussion with Treasury representatives, after which recommendations could be made in the light of that discussion.

Thereupon the meeting recessed and reconvened at 2:35 p.m., with the same attendance as during the morning session, except that Mr. Gidney, an alternate member of the Federal Open Market Committee, was in attendance and Mr. Ransom was not present.

For the purpose of furnishing a market background for the matter under consideration Mr. Rouse stated that at the present time the supply of certificates in the market was quite large and yields were higher than anything the Committee had had in mind in relation to the pattern of rates; that it had been necessary to purchase an additional $65,000,000 of certificates up to this point today and that it would be some time before the situation was relieved, even if large purchases for System account were continued. He also said that the pressing demand for the 2 per cent bonds declined just before the last meeting of the Federal Open Market Committee and that there was no problem in that area and there would not be from all that could be seen over the next several months. He added that when Treasury certificates were first issued in 1942 they had an initial yield of .83-.81 per cent, and that the adoption of a procedure such as that suggested in the memorandum which he sent to Mr. Sproul under date of December 1, 1944, which would provide a yield ranging from .50 per cent on three months' certificates to .78 per cent on twelve months' certificates would involve a premium during the nine months' period of not to exceed 3/32s so that the profit to be realized by holders from sales of certificates would be negligible in amount.

Chairman Eccles said that until some decision was made by the Federal Open Market Committee on the larger problems involved it should give the executive committee instructions as to further purchases of Treasury certificates, and in that connection he repeated the substance of the statement which he had made at the meeting of the executive committee this morning with respect to the telephone conversation which he had had with Mr. Bell regarding the present basis on which certificates were being purchased for the System account.

Mr. McKee suggested that there was no reason why the System should guarantee a profit on issues of Government securities with maturities of less than one year and that, as long as the System saw to it that these issues did not fall below par, the Treasury should be satisfied, particularly since they could be used as collateral for borrowing from the Federal Reserve Banks at a rate of 1/2 per cent.

Mr. Sproul stated that there had been a misunderstanding at the Treasury from the very beginning with respect to the extent to which the agreed pattern of rates applied to the short-term market. He also said that the System's commitment was to maintain about the present general level of prices and yields and that the Treasury had applied that to a pattern beginning at 3/8 per cent for Treasury bills but that the Federal Open Market Committee had never agreed to that interpretation of its commitment. He felt that, in order to avoid the charge of the Committee failing to live up to its commitment, the matter should be taken up with the Treasury so that it would know what the decision of the Committee was in connection with it.

At the conclusion of the discussion, upon motion duly made and seconded, and by unanimous vote, it was decided to make no change in the policy which had been followed in the recent past with respect to purchases of Treasury certificates.

In taking this action it was understood that the executive committee would advise the Federal Reserve Bank of New York of the Committee's decision and that Chairman Eccles would advise Under Secretary of the Treasury Bell of the decision and the reasons therefor.

Upon motion duly made and seconded, and by unanimous vote, the executive committee was requested to meet after the first of the year for the purpose of considering the proposals contained in the memorandum presented by Chairman Eccles and the comments made at this meeting in connection with them, and, if the executive committee could agree upon a recommendation, to submit it to the Treasury for consideration.

Following a review of the general open market policies now in effect there was unanimous agreement that there was nothing in the existing situation that called for any change in these policies at this time and that, therefore, no change should be made in the direction issued to the Federal Reserve Banks at the meeting of the Federal Open Market Committee on March 1, 1944, with respect to the purchase of Treasury bills at a discount rate of 3/8 per cent per annum.

Upon motion duly made and seconded, and by unanimous vote, the following direction to the executive committee was approved, with the understanding that the limitations contained in the direction would include commitments for purchases and sales of securities for the System account.

That the executive committee be 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 practical administration of the account, or for the purpose of maintaining about the present general level of prices and yields of Government securities, or for the purpose of maintaining an adequate supply of funds in the market; provided that the aggregate amount of securities held in the account at the close of this date [other that (1) bills purchased outright in the market on a discount basis at the rate of 3/8 per cent per annum and bills redeemed at maturity and (2) 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 $1,500,000,000.

That the executive committee be further directed, until otherwise directed by the Federal Open Market Committee, to arrange for the purchase for the System open market account direct from the Treasury 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 amount of such certificates held in the account at any one time shall not exceed $1,500,000,000.

At this point Mr. Rouse reported that he had just had a further telephone conversation with the Federal Reserve Bank of New York and had learned that it had been necessary to purchase a total of $90,000,000 of Treasury certificates so far today. He also said that he had given instructions to continue to purchase freely any certificates that were pressing for sale at present prices. There was a brief discussion of Mr. Rouse's report and it was agreed that his instructions were in line with the present policy of preventing a further rise in certificate yields.

Reference was then made to the agreement reached at the last meeting of the Committee in connection with the adoption of the revised formula for the allocation of securities in the System account, that pending further action by the Federal Open Market Committee, Treasury bills should not be allocated to any Federal Reserve Bank in an amount that would reduce its reserve ratio below 45 per cent on statement and reallocation dates. It was stated that the present combined ratio of the Federal Reserve Banks was between 49 per cent and 50 per cent, that it would decline further before the next meeting of the Committee, and that it might be desirable at this time to provide for some further leeway for the allocation of bills in the System account.

Mr. Rouse stated that the allocation procedure was working smoothly and would not become a problem before the next meeting.

Mr. Sproul suggested that the matter be referred to the executive committee with the understanding that the present basis of allocation would be continued until it appeared to the executive committee desirable to make a change, when the executive committee would advise the Federal Reserve Banks that, pending further action, bills would not be allocated to any Federal Reserve Bank in accordance with the existing formula in an amount which would reduce its reserve ratio below 43 per cent.

Upon motion duly made and seconded, and by unanimous vote, Mr. Sproul's suggestion was approved.

Following a discussion of possible dates for the next meeting of the Federal Open Market Committee, there was unanimous agreement that the next meeting should be held on February 28, 1945, followed by a meeting on March 1, 1945, in accordance with the procedure followed last year.

Thereupon the meeting adjourned.

Chester Morrill
Secretary.

Approved: M S Eccles
Chairman.