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 Friday, February 29, 1952, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Sproul, Vice Chairman
Mr. Evans
Mr. Gidney
Mr. Gilbert
Mr. Leedy
Mr. Mills
Mr. Powell
Mr. Robertson
Mr. Szymczak
Mr. Vardaman
Mr. A. H. Williams

Mr. Carpenter, Secretary
Mr. Sherman, Assistant Secretary
Mr. Vest, General Counsel
Mr. Thomas, Economist
Messrs. Bopp, Irons, Thompson, Tow, and John H. Williams, Associate Economists
Mr. Rouse, Manager, System Open Market Account
Mr. Thurston, Assistant to the Board of Governors
Mr. Youngdahl, Chief, Government Finance Section Division of Research and Statistics, Board of Governors
Mr. Arthur Willis, Special Assistant, Securities Department, Federal Reserve Bank of New York

Messrs. Leach, Young, Bryan, and Earhart, alternate members of the Federal Open Market Committee

Messrs. Erickson, Johns, and Peyton, Presidents of the Federal Reserve Banks of Boston, St. Louis, and Minneapolis, respectively

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the Federal Open Market Committee held on November 14, 1951, were approved.

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 meetings of the executive committee held on November 13-14, 1951, and February 11, 1952, were approved, ratified, and confirmed.

Before this meeting there had been sent to the members of the Committee a report of open market operations prepared at the Federal Reserve Bank of New York covering the period November 14, 1951 through February 25, 1952, inclusive. Mr. Rouse presented a supplementary report covering commitments executed on February 26-28, 1952, inclusive, and commented briefly on both 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 for the period November 14, 1951, to February 28, 1952, inclusive, were approved, ratified, and confirmed.

Reference was made to the report prepared by Mr. Rouse under date of January 23, 1952, with respect to dealer commissions on transactions for the System open market account, as presented and discussed at the meeting of the executive committee on February 11, 1952. As recommended at that meeting, copies of the memorandum had been sent to the Presidents of all Federal Reserve Banks for their information and for such discussion at this meeting as might appear to be desirable.

None of the members of the Federal Open Market Committee and none of the Presidents of the Federal Reserve Banks who were not members of the Committee had any comments to make concerning the memorandum, and it was ordered received and filed.

At Chairman Martin's request, the Secretary reported on a change in the procedure for forwarding investment schedules pertaining to the System open market account from the Federal Reserve Bank of New York to the Division of Examinations of the Board of Governors currently in connection with the examiners' audit of the System account. Mr. Carpenter stated that this change was made in January of this year with the thought that much of the detailed work of the examiners which heretofore has been accomplished with borrowed help at the New York Bank during the examiners' audits of the System open market account could be done in the Board's Division of Examinations on a current basis, and that the investment schedules which previously had been set aside at the Federal Reserve Bank of New York for the use of the Chief Federal Reserve Examiner at the time of his examination of the Bank were now being forwarded to the Board on as nearly a weekly basis as possible. Members of the Committee noted the change without objection.

Members of the staffs of the Board's Division of Research and Statistics and Division of International Finance then presented an economic review and outlook illustrated by chart slides. At the close of the review, Mr. Thomas made a statement with respect to credit and monetary policies in relation to fiscal and debt management problems.

In his remarks, Mr. Thomas said that the economic picture was one of approximate balance at high levels of activity, that this situation had prevailed for nearly a year during which there had been an important measure of credit restraint, and that there now were in prospect some factors suggesting the possibility of downward readjustments in prices and decreases in some phases of business activity. There are also in prospect, however, a number of factors that would tend to generate inflationary pressures, particularly the expanding defense program and the continued high level of capital expenditures by business. With the Federal fiscal position shifting from a cash surplus to a sizeable cash deficit which would be at least $4 billion for the calendar year 1952, the Government might need to borrow as much as $10 billion during the second half of 1952 in order to meet the deficit and cover cash redemptions of maturing securities. Mr. Thomas felt that unless individuals and corporations put relatively more of their liquid savings into Government securities and held smaller cash balances, there might need to be an expansion of bank credit, possibly as much as $4 billion, to bring the volume of credit in line with potential demand. This would add to the money supply and be an inflationary influence.

Under circumstances recently prevailing and in prospect, Mr. Thomas felt that continuation of Federal Reserve policies of neutrality would be particularly appropriate since under those policies monetary and credit restraint or ease results from the interplay of market forces of demand and supply with a minimum of Federal Reserve intervention. Thus, if borrowing demands should turn out to be less than the supply of savings available for investment, the money market should be relatively easy and there would be little occasion for the System to try to prevent the ease from occurring. On the other hand, should combined borrowing demands from Government and private sources exceed the supply of savings and call for much bank credit expansion, a tighter market should be expected unless the Federal Reserve intervenes to supply reserve funds. Only in case forces of recession or inflationary pressures become overwhelming should there be need for positive and vigorous action by the System to operate against the trend of borrowing demands, Mr. Thomas felt, and principal reliance should be placed on member bank borrowing as a means of obtaining additional reserves.

With respect to financing the prospective deficit, Mr. Thomas stated that it was impossible to provide easy credit for Government without at the same time making easy credit available to private borrowers. There should be a positive program of debt management aimed at attracting nonbank funds to meet the deficit. An improved savings bond program and offerings of other securities attractive to individuals would be needed to attract savings into Government securities.

While additional restrictions on credit seemed unnecessary at present, Mr. Thomas expressed the view that relaxation of restraints was not called for and measures should continue in readiness to restrain any resumption of inflationary tendencies.

Following Mr. Thomas' comments, Mr. Powell stated that it appeared that during 1951 an important measure of restraint had been exercised by the public through its willingness to save at a high rate but that if the public were to resume spending at a substantially higher rate during coming months, upward pressure on prices would be renewed. Under these circumstances, Mr. Powell asked what the Committee might do in the field of monetary and credit policy to offset the increased spending.

Mr. Thomas commented that in that situation vigorous action to reduce the supply of funds would be desirable.

Mr. Sproul stated that he felt it was possible to place too much emphasis on the role of consumer spending. He also said that while consumer restraint in spending had been an important factor in the relative price stability over the past year, it was his opinion that no small part of the willingness of consumers to save reflected a belief that measures were being or might be taken to preserve the purchasing power of the dollar, and that if consumers continued to believe appropriate measures in that direction would be taken there would be a continuation of savings. On the other hand, if the public began to feel that proper fiscal and debt management and monetary policies were not being pursued and that there was a likelihood of renewed inflationary movements, the incentive to save would be reduced. Mr. Sproul said that in that case the remedy prescribed by Mr. Thomas--vigorous action to reduce the supply of funds--would not be easy to apply. Whatever the reasons, Mr. Sproul said, it was becoming increasingly apparent that the country would not have an adequate fiscal policy in that there would be a large Federal deficit at a time when the budget should be balanced. In the field of debt management, the Treasury faced a need for substantial borrowings to finance the deficit during the last half of the calendar year 1952, at the same time that it would be almost constantly in the market with refunding operations. This may well preclude a vigorous credit policy, so that if the public does not continue to save a difficult problem will be presented. Under these circumstances it was Mr. Sproul's view that it is necessary to begin immediately to pursue a bold, vigorous program for obtaining funds from nonbank sources wherever possible and that both an improved savings bond program and a more effective program of sales of Government securities to nonbank investors would be needed to accomplish this purpose. The problem ahead appeared to him to be a very difficult one which could be quite intractable in terms of an adequate credit policy if there were not a complementary problem of debt management.

Chairman Martin commented that he felt some encouragement could be found in the program undertaken by the Treasury in connection with its March refunding although he did not minimize the difficulties outlined by Mr. Sproul in his comments. He felt that the Committee should take advantage of the period prior to the refunding of the July certificates to work out a further program with which to attack the problem. In this connection, he referred to the memorandum on Government Financing in 1952 prepared by the System Research Committee on Government Finance under date of January 25, 1952, copies of which were sent to all members of the Committee before this meeting, and at his request Mr. Youngdahl summarized the comments appearing in that memorandum on pages 17-23 regarding types of long-term securities that might be offered by the Treasury.

Following Mr. Youngdahl's statement, Mr. Sproul said that he felt that, even under existing circumstances, a long-term unrestricted marketable bond was preferable to a nonmarketable convertible issue, as it would be the means by which the Treasury could raise the largest amount of long-term funds from nonbank sources at the lowest cost. While there were risks in undertaking long-term financing in the situation which faces us, he felt that they were necessary in order to do the financing in a manner that would not be inflationary and that would avoid greater risks of doing an unsatisfactory job of attracting nonbank funds. He recognized that prices of existing issues would decline but felt that the extent of the decline would be limited by the willingness of existing holders to sell at a loss. He thought this sort of market adjustment preferable to trying to cushion the effects of long-term financing by a nonmarketable convertible issue. Such issues, he said, would establish an undesirable mechanical connection between short- and long-term rates and would, in effect be a trap for the investor who might buy without full realization of the conditions and penalties of liquidation. He also said such issues would take control of the debt structure out of the hands of the Treasury because it would not know whether it had a thirty-year or five-year obligation outstanding. He added that, although the convertible issue offered by the Treasury last year was a desirable means of meeting the problem confronting the Treasury and the System at that time, the issue should not be further imbedded into the debt structure and should not be recommended to the Treasury as a way out of the dilemma of getting long-term funds as a supplement to an improved savings bond program.

During Mr. Sproul's statement Mr. Riefler, Assistant to the Chairman, Board of Governors, joined the meeting.

There was a further discussion of the advantages of marketable and nonmarketable issues during which Chairman Martin inquired if the members of the Committee had any views that differed from those expressed by Mr. Sproul. No further comments were made whereupon Chairman Martin suggested that the members of the Committee continue to study the problem presented in the memorandum prepared by the System Research Advisory Committee, that the full Committee ratify the action of the executive committee in sending a copy of the memorandum to the Treasury, and that the Treasury be advised that, after considering the memorandum, the Federal Open Market Committee agreed that use of a marketable security at a competitive rate would be preferable to the use of a nonmarketable convertible issue in Treasury long-term financing operations later this year.

There was also a discussion of other questions relating to Treasury financing including possible new money financing during May of this year and question was raised as to whether the Treasury might find it desirable to use tax anticipation bills similar to those issued in the fall of 1951. There was also a discussion of whether payment for such bills, if issued, should be permitted through credit to tax and loan accounts of banks or whether they should be sold only to corporations (including banks) which might use them in payment of their own taxes. Chairman Martin said that these were matters in which the Committee should work closely with the Treasury.

Mr. Sproul expressed the view that, if possible, it would be desirable not to go to the market for new money in May or June of this year, particularly since large refinancing operations would become necessary in July and new money financing would be necessary during the second half of this year. If it should become necessary for the Treasury to obtain new money before the end of June, Mr. Sproul suggested the possible use of the authority of the Federal Reserve System to purchase direct from the Treasury short-term certificates of indebtedness for the temporary accommodation of the Treasury.

Chairman Martin suggested that the question of a recommendation to the Treasury on this point and other matters relating to Treasury financing be left to the executive committee, that the Committee ratify the transmission to the Treasury of the memorandum on Government Financing in 1952, and that the Treasury be informed that the Committee would favor long-term financing by means of a marketable issue rather than a nonmarketable convertible issue.

This suggestion was approved unanimously.

Chairman Martin then referred to a memorandum dated February 25, 1952, with respect to the establishment of rates on purchases of bankers' acceptances which had been sent to all members of the Committee together with an opinion by Mr. Vest concerning the establishment of such rates by the Federal Open Market Committee. At the Chairman's request, Mr. Carpenter reviewed the circumstances which gave rise to the memorandum, stating that when the currently effective buying rates for acceptances were increased by the Federal Reserve Bank of New York in December 1951 in accordance with a rise in dealers' rates, some of the other Reserve Banks, instead of establishing a schedule of currently effective rates, presented to the Board of Governors for approval an increase to 1-7/8 per cent in their authorized minimum buying rate. As a result of discussions at that time, he said, it was agreed that consideration should be given at this meeting to the procedure to be followed in the future.

Chairman Martin suggested that the matter be referred to the executive committee with a view to having it submit a recommendation at the next meeting of the full Committee.

This suggestion was approved unanimously.

There followed a general discussion of open market policy during which Chairman Martin commented upon the possible need for additional bank credit to carry inventories incident to rescheduling of defense production. At the conclusion of the discussion it was unanimously agreed that no change should be made in the Committee's current policy of neutrality in the market under which market forces of supply and demand are permitted to have their effect with a minimum of System intervention except to the extent necessary to promote orderly market conditions.

Thereupon the meeting adjourned.

S. R. Carpenter

Secretary.