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 8, 1952, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Sproul, Vice Chairman
Mr. Bryan
Mr. Earhart
Mr. Evans
Mr. Hugh Leach
Mr. Robertson
Mr. Vardaman
Mr. C. S. Young

Mr. Riefler, Secretary
Mr. Thurston, Assistant Secretary
Mr. Vest, General Counsel
Mr. Thomas, Economist
Messrs. Mitchell, Roelse, Wheeler, C. W. Williams, and R. A. Young, Associate Economists
Mr. Rouse, Manager, System Open Market Account
Mr. Sherman, Assistant Secretary, Board of Governors
Mr. Youngdahl, Assistant Director, Division of Research and Statistics, Board of Governors
Mr. Willis, Assistant Secretary, Federal Reserve Bank of New York

Messrs. Erickson, Gidney, Johns, and Powell, alternate members of the Federal Open Market Committee

Messrs. A. H. Williams, Leedy, and Gilbert, Presidents of the Federal Reserve Banks of Philadelphia, Kansas City, and Dallas, respectively.

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the Federal Open Market Committee held on September 25, 1952, 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 September 15, September 25, October 8, October 22, November 5, and November 25, 1952, were approved, ratified, and confirmed.

Before this meeting there had been brought to the attention of each member of the Committee a report of examination of the System open market account as of October 17, 1952, made in connection with the regular examination of the Federal Reserve Bank of New York and submitted by the examiner in charge for the Board of Governors. The report took no exception to the handling of the account and stated that the accounting procedures, records, system of internal control, and degree of care exercised by the Federal Reserve Bank of New York in connection with the System open market account were reviewed and continued to be regarded as satisfactory.

Upon motion duly made and seconded, and by unanimous vote, the report was received and ordered filed.

A report of open market operations prepared at the Federal Reserve Bank of New York covering the period September 25 to December 3, 1952, inclusive, had been sent to all members of the Committee before this meeting and at this time there was presented a supplementary report covering commitments executed on December 4 and 5, 1952. Mr. Rouse commented briefly on both reports, copies of which 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 September 25 to December 7, 1952, inclusive, were approved, ratified, and confirmed.

At this point, members of the staff of the Board of Governors entered the room to assist Messrs. Thomas and Ralph Young in presenting a review of the economic situation and credit outlook. The review pointed out that high level economic stability had continued during the autumn with activity and employment advancing to higher levels than last spring and with prices not advancing. There was some evidence that the peak of the defense program in terms of requirements for materials and manpower is close at hand, and that the rise in public expenditures in the next six months would be much less than expected earlier. On the other hand, if problems in Korea or elsewhere should become more serious than heretofore, military expenditures might resume a rapid rise. In either case, continuation of acute international uncertainties may have the result of encouraging many businesses to hold larger inventories and more standby capacity than otherwise. Government policies on stock piling and production capacity goals will also continue to reflect the uncertainties of the foreign situation. Because of these uncertainties and for other reasons, there will probably be heavy pressure on the Federal Government to do everything possible to avoid any marked decline in economic activity.

With respect to the credit situation, the review stated that total credit demand had been at record peacetime levels this year reflecting particularly Federal deficit financing during the last half of the year and that the recent accelerated bank credit expansion was a matter of concern in view of the economy's present intensive use of its physical resources and the large volume of credit already outstanding. While monetary expansion, partly because of a greatly enlarged savings supply, had been held to moderate limits this year, the economic outlook beyond the next few months was by no means clear. Accordingly, the review stated that credit and monetary policy would need to be kept alert to realignments in underlying forces that might affect long-term growth and stability so that it could be adjusted promptly and effectively to changing conditions as they develop. It was felt that the progress made during the past two years in redeveloping a pattern of Federal Reserve operations based on traditional procedures, adapted to a market in which Government securities play a prominent role, provides a workable basis for future credit and monetary policies geared to the needs of a dynamic economy.

During the discussion regarding the presentation, Mr. Ralph Young, in response to a question, stated that, while current information on inventories of manufacturers and distributors was rather sketchy, available data indicated there had been some further development of inventory accumulation during the month of November. He added that the increase resulted to some extent from the fact that many concerns probably desired to carry larger inventories at this time as a safeguard against possible shortages that might develop if the international situation worsened, but that the inventory accumulation also reflected expanding private demands for final products.

Chairman Martin then referred to a memorandum prepared in the offices of the Board of Governors under date of December 8, 1952 on the outlook for Treasury cash requirements and bank reserves, copies of which were distributed before this meeting. In response to the Chairman's request, Mr. Youngdahl commented upon this memorandum, stating that although it referred to an estimated Treasury cash deficit for the fiscal year ending June 30, 1953 of about $3.5 billion, there was now some feeling among informed persons in Washington that the actual cash deficit might be below this figure. The situation had changed primarily, Mr. Youngdahl said, as a result of lower-than-anticipated expenditures for security purposes.

In response to the Chairman's request, Mr. Thomas commented that in recent weeks the demand for credit and particularly for currency had been greater than amounts projected earlier this fall as representing moderate seasonal demands. The net result had been that Reserve Bank credit other than float had risen about $1-1/4 billion in the September-November period compared with the earlier estimate of $800 million. The difference had been reflected in an increase of member bank borrowing to over $1-1/2 billion. The task for the next few weeks, Mr. Thomas said, was to take care of holiday and year-end demands, smoothing out any money market strain.

He thought that strain probably had reached a peak during the past week, and that, if the expected increase in Federal Reserve float took place between now and Christmas, borrowings from the Reserve Banks could be reduced somewhat. There would be a temporary strain in the market at the year-end, after which the return flow of currency would make for easier conditions in the money market, but reduction in the large volume of member bank borrowing and of repurchase contracts outstanding would absorb a substantial amount of the reserve funds that would become available. The question then, Mr. Thomas felt, would be the extent to which the System would wish to maintain a tight rein on the situation by permitting bills to run off, and perhaps by selling certificates if there were an opportunity. Additional restraint could be imposed upon future demands by increasing the discount rate.

Chairman Martin referred to the statement by Mr. Sproul contained in the minutes of the meeting of the executive committee for November 25, 1952 with respect to the possible desirability of a change in the discount rate and suggested that there be a further discussion of that question at this meeting of the full Committee both as related to the immediate situation and the situation that would exist after the turn of the year.

Mr. Hugh Leach stated that the situation at the year-end in 1951 had presented considerable difficulty, that this year borrowings from the Reserve Banks were much higher than a year ago, and that if the discount rate were raised between now and the first of the year it would increase problems in the money market and would make it necessary for the System to purchase additional securities which was something to be avoided. He felt the System should wait until January to see what changes in prices took place, what inventory developments were indicated, and whether the expected seasonal liquidation of credit occurred before deciding whether an increase in the discount rate were necessary.

Mr. Powell raised the question whether the quality of credits of member banks may have deteriorated with declines in prices for products collateraling such credits. He cited instances of increases in farm mortgage debt recently for the purpose of securing farm loans that were undercollateraled because of declines in livestock prices, and of the concern on the part of some bankers because underfinanced companies were building up inventories and borrowing on receivables. Mr. Powell felt that this situation might be considered in a discussion whether the discount rate should be increased, adding that a small increase in the rate would not upset the market and might be a warning that the Federal Reserve System thought collections on loans ought to be watched. He also suggested that such a warning might be given now rather than waiting until after the first of the year.

Mr. Evans commented on conditions he had observed in the Middle West during the past two weeks, stating that on the basis of his observations, Mr. Powell's description of conditions in that area was, if anything, an understatement of the situation; that some of the bankers he had talked with stated that a good deal of livestock paper now represented 100 per cent loans based on present prices. Mr. Evans felt the Committee had been a little too lax in permitting credit to expand as much as had taken place during the past six to eight months. He thought it a question, however, whether the Committee should now tighten credit very much in view of the conditions prevailing in the Midwest as a result of the drought, declines in cattle and other farm products prices, and accumulating inventories of dealers and manufacturers of farm equipment.

Mr. C. S. Young stated that while he agreed with Mr. Powell as to the need for studying the quality of credits, he felt the redeeming factor was that member banks were aware of this situation, that they were doing a remarkable job of weeding out poor loans and of securing additional collateral; on the whole, he felt the banks were in good condition although the quality of some loans had deteriorated.

Mr. Leedy stated that the drought was a serious factor in the Kansas City District and, although conditions had been improved somewhat by moisture during the past two weeks, the winter wheat crop for next year would be small. With respect to cattle loans, most such paper being offered the Kansas City Reserve Bank for discount indicated there was still a satisfactory margin of collateral.

Mr. Earhart said that activity on the Pacific Coast appeared to be running a little ahead of the national level at this time reflecting a continued inflow of population plus the inflow of funds resulting from transfers of funds of individuals and payments by the Federal Government for aircraft, the aggregate of which exceeded the outflow of funds from the Twelfth District. Building was very active, particularly in the southern part of the district, and while one of the largest banks felt the outlook for the entire year 1953 was good another bank which had been making large volumes of real estate loans was beginning to feel that there were real dangers ahead, particularly in the real estate market. Mr. Earhart said that he would go along with the view that there should be no change in the discount rate now but that he felt it was too low, that it should have been increased before this, and that after the turn of the year there might be reasons which would make it seem about as untimely to increase the rate as the present.

Mr. Gidney commented on the discussion recorded in the minutes of the November 25 meeting of the executive committee, stating that in his judgment the reasons for an increase in the discount rate, as summarized by Mr. Sproul, were much more convincing than the reasons presented for not increasing the discount rate promptly. The high level of bank loans, the fact that Federal Reserve credit in use had gone up recently while the Committee apparently was operating on a policy of "neutrality", and recent economic developments (other than the modest change in wholesale prices) pointed clearly to the desirability of an immediate increase in the discount rate. He added that the present offered a better opportunity than is likely to occur for some time for making such an increase without disturbing the market unduly, while after the turn of the year reasons against making a change quite probably would develop or be advanced, including those related to interference with Treasury refunding operations.

Chairman Martin stated that he seriously questioned the desirability of an increase in the discount rate at this time. The period over the year-end would be difficult in any event because of disturbed conditions in the money market and uncertainties as to the credit outlook; to take action at present would only add to the upset condition in the market and probably would achieve little in the way of affecting the differential between the discount rate and the bill rate. If, following January 1, conditions did not bring about liquidation of the credit that had been extended this fall, it would be desirable to give consideration to an increase in the discount rate at that time.

Mr. Bryan said that while he had no argument to present for a change in the discount rate at this time, it seemed somewhat absurd for the central bank to have a discount rate of 1-3/4 per cent at a time when plant and labor supplies of the country were being utilized virtually at capacity. He felt that the Committee had been in a self-congratulatory mood over the past year in taking the view that the country was having stability at a high level. But unemployment now was negligible, and Mr. Bryan felt this could not persist without a rise in prices. He wondered, therefore, whether the Committee's policy had been sufficiently restrictive.

Mr. Sproul felt that the price level had reflected a relatively stable economic situation up to now and that the policy of the System, whatever its influence, had been consistent with a stable price level and a high level of economic activity. Unless it was felt that credit restraint should have been used to bring about an actual decline in prices, he did not see how the "high level stability" during the period under discussion could be considered a criticism of the policy pursued. Looking ahead, Mr. Sproul felt that two points of view, perhaps paradoxical, had been raised: first, there was the view that the general outlook was for a high level of income and production over the next three to six months with no immediate evidence of price inflation although there was some evidence of inventory accumulation. This view suggested that the Committee should remain on the alert, but it did not call for action at this time. The other point of view, Mr. Sproul said, was that there were some elements in the situation which suggested disintegration in the area of bank credit such as loans which were becoming undercollateraled because of agricultural production difficulties and prospective or present declines in the agricultural outlook and prices. This might suggest a relaxation instead of a tightening of credit policy. To some extent, Mr. Sproul said, the System was a prisoner of the fact that it was just working back into the use of the discount rate and flexibility in that rate. It had laid great emphasis on the meaning of a change in the discount rate, and a move now might be regarded as symbolic of a change in the general economic situation rather than a technical readjustment. Mr. Sproul doubted whether an increase of one-fourth or one-half of one per cent--which was all that he assumed anyone would suggest at this time--would accomplish anything in the next two or three weeks except to complicate adjustments in the year-end money market.

Mr. A. H. Williams stated that in the Philadelphia district the most general view was that a change in the discount rate should not be made until there had been an opportunity to observe developments after the turn of the year so as to be more certain whether a change was needed.

Mr. Gilbert said he would not be in favor of an increase in the discount rate at this time, that he would much rather wait until after the end of the year to observe whether the normal repayment of borrowings that had developed this fall took place; if the seasonal liquidation in loans did not take place, he thought consideration then should be given to an increase in the rate.

Mr. Erickson agreed with this view.

Mr. Bryan reiterated the comment that while he did not advocate an increase in the discount rate at this time, he thought it an extraordinary event in terms of central banking that the rate remained at 1-3/4 per cent at a time when the economy was operating with virtually full employment, and that such a rate was defensible only in terms of the record of the Open Market Committee over a period of several years.

Chairman Martin commented that it was also important to remember that the present rate had existed in a conjunction of circumstances evident in the return to a freer market in Government securities. He went on to say that, as he had indicated at the meeting of the executive committee on November 25, the Federal Reserve System was in a constant dilemma with respect to the effect of its actions on Treasury financing. At some point it would be necessary to meet this issue head-on; this, he said, should preferably be done in conjunction with the Secretary of the Treasury. He felt that the System should not make a move to increase the discount rate until it was convinced that such an increase was appropriate, but that it should then act even though at that time the System might be faced with the immediate question of the effect of the increase on the Treasury's financing program. The System may have "missed the boat" in not having raised the discount rate some time ago, the Chairman said, but if that were true it still did not warrant taking corrective action at this particular time simply because it might be more difficult to face up to the problem of appropriate monetary policy when Treasury financing was under active consideration early next year. Chairman Martin added that the System had been going through these periods of anxiety, that it had made some progress in its monetary policy, that Mr. Bryan had made an excellent point in suggesting that the Committee not be too ready to congratulate itself, and that Mr. Gidney had brought out a view which it was very desirable to discuss. Nevertheless, Chairman Martin said, the discussion indicated that the Committee should proceed with its present policy, having in mind that it might become necessary to have another meeting of the Committee soon after the first of the year.

There was no indication of disagreement with Chairman Martin's suggestion for continuation of the existing policy of the Committee.

Mr. Sproul noted that speculation regarding a possible change in the discount rate caused disturbance in the money market and suggested that, in so far as possible, discussion of such a possibility not be carried on outside.

Chairman Martin agreed with this suggestion, adding that while it was necessary for the directors of the Reserve Banks to discuss the matter, it would also be desirable for the Reserve Bank Presidents to caution them against discussion of the subject outside the meetings of the directors.

Thereupon, upon motion duly made and seconded, the following direction to the executive committee was approved unanimously:

The executive committee is 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 light of current and prospective economic conditions and the general credit situation of the country, with a view to exercising restraint upon inflationary developments, to maintaining orderly conditions in the Government security market, to relating the supply of funds in the market to the needs of commerce and business, and to the practical administration of the account; provided that the aggregate amount of securities held in the System account (including commitments for the purchase or sale of securities for the account) at the close of this date, other than 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 $2,000,000,000.

> The executive committee is further directed, until otherwise directed by the Federal Open Market Committee, to arrange for the purchase direct from the Treasury for the account of the Federal Reserve Bank of New York (which Bank shall have discretion, in cases where it seems desirable, to issue participations to one or more Federal Reserve Banks) 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 total amount of such certificates held at any one time by the Federal Reserve Banks shall not exceed in the aggregate $2,000,000,000.

In a discussion of a date for the next meeting of the full Committee, reference was made to a memorandum prepared by Mr. Vest dated December 2, 1952, stating that inasmuch as March 1, 1953, will fall on a Sunday, it would seem to be desirable, if otherwise practicable, for the meeting of the new Committee to be held during the first week of March 1953. In commenting on this, Mr. Vest stated that the organization meeting of the new Committee usually had been held on March 1 of each year and that it was customary for a meeting of the old Committee also to be held late in February in order to ratify actions taken up to that time. He said there was no reason why, if ratification is necessary, the new Committee could not ratify actions taken by the previous Committee, and that he did not think it essential that the old Committee meet in late February. Following a discussion, it was agreed that the next meeting of the full Committee should be held during the week beginning March 2, 1953.

Thereupon the meeting adjourned.

Winfield W. Riefler
Secretary