

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 Thursday, October 4, 1951, at 10:05 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Sproul, Vice Chairman
Mr. Gidney
Mr. Gilbert
Mr. Leedy
Mr. Norton
Mr. Powell
Mr. Szymczak
Mr. A. H. Williams

Mr. Carpenter, Secretary
Mr. Sherman, Assistant Secretary
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. Riefler, Assistant to the Chairman, Board of
Governors
Mr. Ralph A. Young, Director, Division of Research
and Statistics, Board of Governors
Mr. Solomon, Assistant General Counsel, Board of
Governors
Mr. Youngdahl, Chief, Government Finance Section,
Division of Research and Statistics, Board
of Governors
Mr. Ralph F. Leach, Economist, Division of Research
and Statistics, Board of Governors
Mr. Arthur Willis, Special Assistant, Securities
Department, Federal Reserve Bank of New York

Messrs. Hugh Leach, C. S. 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.

Mr. Townsend, Solicitor, Board of Governors

Mr. J. Marvin Peterson, Director of Research,
Federal Reserve Bank of Minneapolis

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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 May 17, 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 May 7, May 17, June 27, August 8, and August 27, 1951, 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 May 17 to September 27, 1951, inclusive. Mr. Rouse commented briefly on this report and on a supplementary report covering commitments executed September 28 to October 3, 1951, inclusive, copies of which also were distributed to the members of the Committee. Copies of both 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 May 17 to October 3, 1951, inclusive, were approved, ratified, and confirmed.

Members of the staff of the Division of Research and Statistics of the Board of Governors then presented a report, illustrated by charts, covering the economic situation. Following this report, Mr. Thomas made a statement on the implications for credit policy in the current economic outlook in which he said that during the first four months of the new Federal Reserve policy developments indicated that either the policy was

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effective in restraining further credit inflation or that the abatement of inflationary pressures for other reasons was so great as not to subject the monetary policy to a rigorous test. Mr. Thomas went on to say that there was evidence that credit restraints played some part in curbing inflation, especially in the mortgage market, and that it was likely that had the change in policy not occurred investment institutions would have continued to sell bonds to the Federal Reserve with the result that reserves thus created would have moved into the banks and inducement for credit restraint would have been weakened. Mr. Thomas also said that in this period the money market functioned on its own, that there was little or no increase in total Reserve Bank credit, total bank loans and investments, or total deposits, although the private money supply expanded somewhat because of a reduction in Treasury balances. Within the past three weeks, Mr. Thomas said, the picture had changed drastically and the System had found it necessary to add nearly a billion dollars to its portfolio, reflecting temporary factors such as tax payments, the desire of the banks to avoid borrowing on a statement date, and a lack of enthusiasm for the new Treasury refunding issues. The increase also reflected seasonal loan and currency demands, which would continue during the rest of this year, and the imminence of new cash borrowing by the Treasury, as well as prospective large corporate issues. Mr. Thomas felt that Federal Reserve Open Market purchases at this time, rather than forcing reliance on borrowing by banks to meet reserve needs and permitting interest rates to rise, could be justified on the grounds that some of the demands were of

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a temporary nature and that strong inflationary tendencies were absent at this time.

As for the immediate future, Mr. Thomas said that the large volume of excess reserves now outstanding (about \$1 billion) and the low level of borrowing at the Reserve Banks (less than \$70 million), together with a seasonal expansion in Reserve Bank float, should make it possible that all reserve needs could be met during the remainder of 1951 without any further purchases of securities by the System unless purchases were needed to assure success of new financing offers by the Treasury. Mr. Thomas felt that the large increase in the private money supply that had already occurred and that would continue, together with growing defense expenditures, might result in a resumption of inflationary pressures; if this occurred, the System might wish to adopt more positive measures of restraint. The most promising approach for dealing with the situation would be for the Treasury to offer securities of a type that would compete with other demands and attract the available nonbank funds. Such measures would be even more essential the latter part of 1952 when Treasury borrowing needs probably would be tremendous, and unless those needed funds could be obtained outside the banking system, Mr. Thomas felt further sharp growth in the money supply would result and would present a continuing strong inflationary threat.

There followed a brief discussion of the reports given by members of the Research staff and Mr. Thomas, at the close of which Mr. Townsend withdrew from the meeting.

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Chairman Martin then referred to a memorandum prepared in the Board's offices under date of October 3, 1951, on "Treasury Cash Requirements and Financing, October-December 1951" and to new financing alternatives presented in that memorandum, copies of which were distributed among the members of the Committee prior to this meeting and a copy of which has been placed in the Federal Open Market Committee files.

In response to a request from Chairman Martin, Mr. Rouse made a statement concerning prospective Treasury financing needs during the next few months in which he said that the bill market was congested and was not in a condition to take additional weekly offerings of regular bills, that there was no outside demand for long-term Government securities at the present price level, and that the source of nonbank funds appeared to lie in the tax liabilities of corporations. He felt, therefore, that the Treasury might avail itself of the situation in the short-term money market and sell securities which would be purchased ultimately by corporations for use in paying tax liabilities in the spring of 1952, when the Treasury could repay such borrowings.

Chairman Martin then called upon Mr. Thomas who summarized informal discussions that members of the staff had had with representatives of the Treasury staff. Mr. Thomas said that, while the discussions were exploratory, it was generally agreed that around \$2.5 billion would have to be raised by the Treasury to cover the deficit and attrition in refunding of market issues this fall, that there was rather general agreement this could not be raised by long-term issues, and that most of the funds available

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were funds held by corporations in anticipation of tax payments they would have to make during 1952. One of the proposals under consideration, Mr. Thomas said, was the offering of tax-date bills maturing about March 15 and June 15, 1952; such bills might mature within a few days after these tax payment dates but would be acceptable in payment of taxes on March 15 and June 15. Mr. Thomas also commented upon alternative methods of issuing such securities, stating that some individuals felt they should be issued at one time while others preferred a series of issues coming out over a period of several weeks.

There followed a discussion of the suggestions made in the staff memorandum dated October 3, 1951, and of the comments of Messrs. Rouse and Thomas, including discussion of the terms on which the tax anticipation bills might be issued, at the conclusion of which Chairman Martin suggested that the executive committee be authorized to submit recommendations to the Treasury concerning both refunding and new financing needs, in the light of the discussion at this meeting.

This suggestion was approved
unanimously.

Chairman Martin also referred to a report prepared by the System Research Committee on Government Finance under date of September 28, 1951, on "How the Defense Bond Program Can Be Strengthened", copies of which had been sent to the members of the Committee before this meeting. He suggested that the report be reviewed by the executive committee with a view to having that committee submit a recommendation to the full Committee. He also

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suggested that Mr. Norton be asked to serve with the members of the executive committee in making this review of the savings bond program in view of his interest in and tentative suggestions concerning a more effective program for merchandising bonds.

In connection with a discussion of the time for a meeting of the Federal Open Market Committee at which consideration might be given to matters which should be taken up with the Secretary of the Treasury before the end of this year, including the savings bond program, Chairman Martin suggested that there be a meeting of the full Committee at which Federal Reserve Bank Presidents who were not now members of the Committee would also be present sometime during November 1951. He added that he had discussed the question of possible changes in the savings bond program with Secretary of the Treasury Snyder and that he was under the impression that any recommendations which the Committee might wish to make should be submitted by the latter part of November.

Following a discussion, it was agreed unanimously that a study of the savings bond program should proceed as suggested by Chairman Martin, and that the next meeting of the Federal Open Market Committee, at which the Presidents of the Federal Reserve Banks who were not now members of the Committee would also be present, would be held on Wednesday, November 14, 1951.

In a discussion of open market policy, Mr. Powell expressed the view that the money market, in a variety of ways, was stating the case that interest rates had definitely risen and if the Treasury was going to spread its refundings over a term of years in order to reduce the size of the annual roll-over of debt, it would have to pay the higher

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rates that others were willing to pay. Mr. Powell went on to say that this was the inevitable result of inflationary pressures and the System's attempt to control them with money market instruments, and, after commenting on the factors evidencing upward pressure on the level of rates, he suggested that consideration be given to the question whether it would not be necessary to permit interest rates on Treasury borrowings to rise, if Treasury financing was to be fitted into a situation in which the Open Market Committee continued to exert pressure against inflation through the use of open market instruments.

Chairman Martin stated that Mr. Powell had raised a very pertinent question, that there was a real problem of how effective the System could be in a period of deficit financing in attempting to restrain inflation through open market instruments.

After comments by several Reserve Bank Presidents concerning the attractiveness of long-term Treasury securities to the average saver at existing rates, Chairman Martin called upon Mr. John H. Williams who stated that he shared Mr. Powell's views, that he felt the only way in which the System could overcome inflation was through raising interest rates and thus providing a means by which the Treasury could compete for savings. He felt that this was the way to exert monetary pressure, that it looked as though the country was getting to the end of the road as far as tax increases were concerned except perhaps for a general sales tax, and that the country was confronted with such questions as whether the military program was too large, whether it should be stretched out over a longer period

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of time than was now contemplated, whether it should be financed through use of savings of the country, or whether it would have to be financed by resorting to bank credit.

Mr. Bopp stated that he did not feel the question was one of a deliberate raising of interest rates so much as one of letting the demand for funds force rates up, rather than taking action to prevent a rise.

Mr. Thompson agreed with the comment made by Mr. Bopp, adding that he felt it was unfortunate that the System was too often identified with the proposition of raising interest rates whereas the proposition was basically one of restricting the supply of funds so that those who wanted credit would have to compete for it, which might mean an increase in rates.

Mr. Tow said that any increase in interest rates should be a result of monetary policy rather than a deliberate raising of rates, that the question whether to permit rates to rise was one that would have to be faced in terms of all factors in the situation at a given time, and that it was not particularly significant whether such a change was permitted to occur just after a savings bond sales campaign or at some other time.

Mr. Irons said that the System should not prevent rates from rising if the forces in the market tended to bring about an increase. He expressed doubt that the present rates, certainly those paid on savings bonds, were sufficient to attract savings into Government securities, and he felt that the System should be affirmative to the extent that it should not prevent rates from rising.

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Mr. Peterson felt that it would be a mistake to concentrate on the savings bond rate as such and leave longer-term securities out of consideration.

Mr. Bryan stated that he would like to associate himself strongly with the general line of thought initiated by Mr. Powell and that he did not disagree with most of the comments made subsequently. He added that it seemed to him that in a considerable part of the postwar world, central banks had proceeded on an impression that there would be a savings surplus, whereas, in fact, we had come into a situation where there was a savings deficit. He commented that he did not see any way by which it was going to be possible to avoid further inflation unless, in consort with the Treasury, the central banking system could reach a full recognition of the circumstances in the market and permit an adjustment in the level of rates that would meet the demand. Of the various choices available, Mr. Bryan felt that the best was to face the rate question over a longer term since this was the basic problem, rather than the technicalities as to how short-term financing should be accomplished.

There was a further discussion at the conclusion of which Chairman Martin stated that the problem was one of finding out how to attract new money into Government securities in the period ahead.

Chairman Martin then referred to the authority given to all Federal Reserve Banks on March 1, 1950, which was modified on February 8, 1951, and renewed on March 8, 1951, with respect to repurchase agreements covering short-term Treasury obligations with nonbank dealers in United

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States Government securities qualified to transact business with the System open market account. He stated that question had been raised as to whether the present authority which gave additional leeway to the New York Bank for executing repurchase agreements should be extended to all Federal Reserve Banks.

In the discussion that followed, it was stated that the present authority included the requirement that the rate on such agreements be at least $1/8$ per cent above the average issuing rate on the most recent issue of United States Treasury bills, except that the Federal Reserve Bank of New York was authorized by the actions of February 8 and March 8, 1951, to enter into such agreements at a differential of less than $1/8$ per cent above the average issuing rate on United States Treasury bills. The view was expressed that while this authority would continue to be used primarily if not exclusively by the Federal Reserve Bank of New York, it should be granted to each of the Federal Reserve Banks so that it could be used in the interest of orderly conditions in the Government securities market, and that Federal Reserve Banks other than New York should have the authority in case of an emergency necessitating the transfer of the execution of open market operations to another Federal Reserve Bank.

Following a discussion, upon motion duly made and seconded, it was voted unanimously to authorize each Federal Reserve Bank, in lieu of all similar previous authorizations, to enter into repurchase agreements with nonbank dealers in United States Government securities who are qualified to transact business with the System open market account, under the following conditions:

1. Such agreements
 - a. Are at a rate which will be fixed in fractions of $1/8$ per cent and which ordinarily will be not less than the nearest fraction above the average issuing rate on the most recent issue of 3-month Treasury bills but which at times may be below the average issuing rate on bills but not more than $1/8$ per cent below; (for example, when the issuing rate on Treasury bills temporarily may have risen slightly above the existing repurchase rate);
 - b. Are for periods of not to exceed 15 calendar days;
 - c. Cover only short-term Government securities selling at a yield of not more than the issuing rate for 1-year Treasury obligations; and
 - d. Are used with care and discrimination as a means of providing the money market with sufficient Federal Reserve funds as to avoid undue strain on a day-to-day basis.
2. Reports of such transactions are made to the Manager of the System Open Market Account to be included in the weekly report of open market operations which is sent to the members of the Federal Open Market Committee.
3. In the event Government securities covered by any such agreement are not repurchased by the dealer pursuant to the agreement or a renewal thereof, the securities thus acquired by the Federal Reserve Bank are sold in the market or transferred to the System Open Market Account.

In taking this action it was understood that a letter would be sent to all Federal Reserve Banks advising them of the above understanding.

Reference was made to the decision reached at the meeting of the Committee on May 17, 1951, with respect to conversion of $2-3/4$ per cent nonmarketable bonds held in the system account into 5 year $1-1/2$ per cent marketable notes. Mr. Rouse stated that following out that action

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it would now be appropriate for the System to convert \$500 million of the 2-3/4 per cent bonds into the 1-1/2 per cent notes and that an additional \$500 million should be converted on a similar basis in April 1952 at which time consideration would also be given to the program for conversion of the remaining \$700 million held in the System account. Mr. Rouse went on to say that before carrying out the exchange of \$500 million at this time, it seemed desirable to raise the question whether the Committee wished to make any change in the earlier understanding. He also said that so far as he was concerned in the management of the System account, it would not matter whether the present understanding was carried out or whether the conversion was made in some other manner.

Mr. Szymczak suggested that unless there was good reason for changing the decision reached at the meeting on May 17, it would seem desirable to proceed on the basis of that action.

This suggestion was approved
unanimously.

It was agreed that the executive committee should be authorized to determine, within the limits of the general direction to be issued at this meeting by the full Committee to the executive committee, the basis upon which transactions would be conducted for the System account in bills and other short-term securities. It was also agreed that no change should be made in the existing understanding that operations in longer-term securities should be conducted with a view to maintaining orderly market conditions, in the light of the general direction to be

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issued to the executive committee at this meeting.

Thereupon, upon motion duly made and seconded, the following direction to the executive committee was approved unanimously with the understanding that the limitation contained in the direction would include commitments for the system open market account:

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 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 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 total amount of such certificates held in the account at any one time shall not exceed \$1,000,000,000.

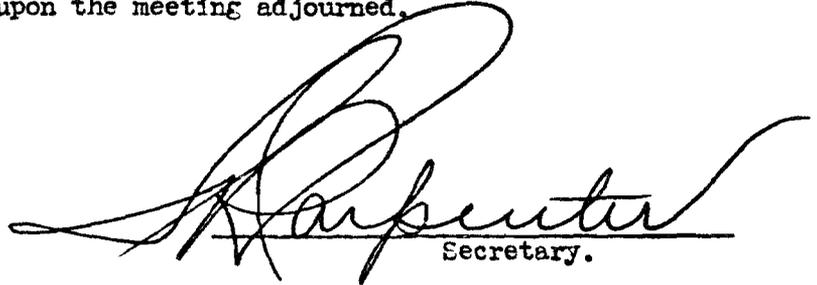
The Secretary stated that he had been advised that the examiners of the Board of Governors of the Federal Reserve System, in connection with the regular examination of the Federal Reserve Bank of New York, had completed an audit of the System open market account and that they had no objections to raise to the handling of the account. He added that the

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customary report of the audit would be distributed among the members of the Committee in the usual manner.

Thereupon the meeting adjourned.



Secretary.