

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 Tuesday, December 15, 1953, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Sproul, Vice Chairman
Mr. Erickson
Mr. Evans
Mr. Fulton
Mr. Johns
Mr. Mills
Mr. Powell
Mr. Robertson
Mr. Szymczak
Mr. Vardaman

Mr. Riefler, Secretary
Mr. Thurston, Assistant Secretary
Mr. Vest, General Counsel
Mr. Solomon, Assistant General Counsel
Mr. Thomas, Economist
Messrs. Abbott, Hostetler, Peterson, Roelse,
Willis, and R. A. Young, Associate
Economists
Mr. Rouse, Manager, System Open Market Account
Mr. Carpenter, Secretary, Board of Governors
Mr. Sherman, Assistant Secretary, Board of
Governors
Mr. Youngdahl, Assistant Director, Division of
Research and Statistics, Board of Governors
Mr. Gaines, Securities Department, Federal
Reserve Bank of New York

Messrs. Leedy, Williams, and C. S. Young, Alternate
Members of the Federal Open Market Committee

Messrs. Bryan, Earhart, and Leach, Presidents of
the Federal Reserve Banks of Atlanta, San
Francisco, and Richmond, respectively

Mr. W. D. Gentry, First Vice President, Federal
Reserve Bank of Dallas

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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 24, 1953 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 24, October 6, October 20, and November 6, 1953, were approved, ratified, and confirmed.

Mr. Robertson stated that before the actions of the executive committee of the Federal Open Market Committee at its meeting on November 23, 1953 were approved by the full Committee he would like to bring up for consideration the matter of "swaps" of Government securities that were authorized by the executive committee at its November 23 meeting. He then made a statement substantially as follows:

Pursuant to that authorization, "swaps" have taken place during the past few weeks by way of sales of issues maturing out to 12-1/2 months and purchases of an equal amount of bills. But before getting to the merits - the basic question of the advisability of "swaps" of this nature - I should like to clear away the possible uncertainty, from a legal point of view, as to whether the executive committee had authority to authorize purchases and sales for the purpose of changing the maturity pattern of the System Open Market Account portfolio.

Since our March 1953 meeting it has been our intention, as I understood it, that open market transactions be confined to purchases and sales for the purpose of releasing or absorbing reserves. The action taken at the June meeting, and rescinded in September, did not affect this basic objective, but related only to our modus operandi in pursuing it.

It is difficult to maintain that the sale, for example, of December 1954 2s and the purchase of equivalent amounts of bills fall within these limits, since such balanced sales and purchases do not release or absorb reserves - they leave the

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volume of reserves at the level which prevailed before the transactions took place.

I have at hand a memorandum which sets forth the grounds on which it might be contended that the authorization of these "swaps" was invalid, with supporting data, but since the entire Open Market Committee is here and can clear up the matter by its action today, there does not seem to be any reason for exploring history. At the same time, since there is no question whatever as to the good faith of the executive committee and the Manager of the Account, there seems to be no good reason for permitting the question of legality or validity of the action to remain in history, possibly to be raised later when the facts are less well in hand.

Therefore, having explicitly raised that question, I wish, before going on to the merits of this problem, and subject to any objections on other grounds, to move that the actions of the executive committee, as revealed by the minutes of its meeting on November 23, 1953, be approved, ratified, and confirmed.

Mr. Robertson's motion was seconded and, following a brief discussion, approved by unanimous vote.

Before this meeting there had been sent to the members of the Committee a copy of a report of open market operations prepared at the Federal Reserve Bank of New York covering the period September 24 to December 9, 1953, inclusive. At this meeting Mr. Rouse presented a supplementary report covering commitments executed from December 10 to December 14, 1953, inclusive, and commented briefly on that report. Copies of both reports have been placed in the files of the Open Market Committee.

Upon motion duly made and seconded, and by unanimous vote, the transactions in the System open market account for the period September 24 to December 14, 1953, inclusive, were approved, ratified, and confirmed.

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Members of the staff of the Board of Governors then entered the room for the purpose of presenting a review of recent business and credit developments, illustrated by chart slides. Copies of the text of the review have been sent to each member of the Committee and a copy has been placed in the files of the Federal Open Market Committee.

Mr. Thurston joined the meeting at the conclusion of the economic review, and, following a brief discussion, members of the staff who had entered the room for the purpose of assisting in its presentation withdrew.

Chairman Martin referred to the report of the ad hoc subcommittee which had been appointed to study operations in the Government securities market and to the discussion of that report at the meeting of the full Committee on March 4-5, 1953. He recalled that at that time two unfinished items of business were referred back to the subcommittee for further consideration, namely (a) the "housekeeping" arrangements and (b) the recommendation of the subcommittee that repurchase facilities at an appropriate rate and with appropriate limitation as to volume be made regularly available to nonbank dealers over week-ends. The ad hoc subcommittee was instructed to meet with Mr. Sproul for the purpose of discussing the housekeeping arrangements covered in the subcommittee's report; and, with respect to repurchase facilities, it was requested to review the recommendation set forth under (b) in terms of the problem of orderly markets and of making reserve funds available on an automatic basis.

Chairman Martin stated that the ad hoc subcommittee met with Mr. Sproul on October 20, 1953 for the purpose of discussing housekeeping

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arrangements. He noted that in its original report the subcommittee had made no recommendation concerning housekeeping arrangements other than to suggest that the full Committee re-examine and review the structure of its organization. He stated that at the meeting on October 20 at which Mr. Sproul was present there was a discussion of all aspects of the housekeeping problem in a manner which had been useful and constructive. As a result of that discussion, Chairman Martin said, the subcommittee decided to make no additional recommendations at the present time. It also agreed that the problem should be returned to the full Committee with the thought that such matters as the budget for operating the open market account, management of the account, the responsibility of management, and the modus operandi would be reviewed by the full Committee from time to time. Chairman Martin referred in this connection to the letter addressed by Mr. Sproul to each member of the Committee under date of December 7, 1953 which presented information concerning the organization of the securities function at the Federal Reserve Bank of New York and the management of the System account, including data with respect to the expense of operation of the account. He felt that the information contained in Mr. Sproul's letter made a useful contribution to the study of the problem and he noted that Mr. Sproul's letter extended an invitation to all members of the Federal Open Market Committee to visit the New York Bank to observe the actual operations of the account.

Chairman Martin stated that in suggesting that the housekeeping problems be returned to the full Committee, it was not intended to eliminate

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review and study of these problems. He urged that each member of the Committee and appropriately designated staff members arrange to go to New York as opportunity offered and spend some time observing the operations of the account and the problems of its management, the responsibility for which was shared by all members of the Committee. Chairman Martin also said that he would like to have members of the Committee who were able to visit New York comment on the operation at forthcoming meetings of the full Committee.

With respect to the question of repurchase agreements, Chairman Martin said that the use of such agreements was a running problem and the ad hoc subcommittee would like to have it returned to the full Committee for whatever study seemed warranted. He referred to a memorandum which had been prepared by Messrs. Riefler and Thomas for distribution to all members of the Committee under date of December 9, 1953 on the use of repurchase contracts to meet temporary reserve needs in December of this year. (A copy of this memorandum has been placed in the files of the Federal Open Market Committee.) Chairman Martin felt the questions raised in the memorandum warranted study by the Committee but he did not think they could be decided at this meeting. He suggested that there be a discussion of this matter later during this meeting as well as of a letter addressed by Mr. Sproul to each member of the Committee under date of December 4, 1953 (a copy of which has been placed in the files of the Committee) commenting on the action taken by the full Committee at its meeting on September 24 in approving a motion

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by Mr. Mills that operations for the System account be confined to short-term securities (except in the correction of disorderly markets) and that the System account refrain from certain transactions in Treasury securities during a period of Treasury financing.

Chairman Martin went on to say that Mr. Sproul's letter of December 4 set forth clearly and explicitly the position he had understood Mr. Sproul to hold but that it did not alter his (Chairman Martin's) views regarding the desirability of confining operations to short-term securities and refraining from dealing in certain securities during Treasury financings. The Chairman also said that he had asked the staff to gather additional data as to the recent performance of the Government securities market about which Mr. Sproul had commented in his letter. Such material would be sent to the members of the Committee for their further consideration, Chairman Martin said, even though statistics might not be conclusive in indicating the validity of the position he had taken in his letter to the members of the Committee of September 15, 1953, nor would they necessarily carry out the points made by Mr. Sproul in his letter of December 4. He thought it would be desirable, however, for the members of the Committee to consider and study the information that had been submitted and would be submitted in this connection.

Secretary's note: A memorandum from Chairman Martin presenting additional data regarding pressure on the market during periods of refunding was sent to the members of the Committee at the time these minutes were distributed, and a copy has been placed in the files of the Federal Open Market Committee.

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Chairman Martin emphasized that the problems which had been presented in the ad hoc subcommittee report and which had been covered in Mr. Sproul's letters of July 16 and December 4, 1953, and in his (Chairman Martin's) letter of September 15 were problems which must be continually kept under study by the members of the Committee. He felt, he said, that the study made by the ad hoc subcommittee had fulfilled its purpose; as a member of the full Committee, he was encouraged by the amount of discussion that had been engendered by the subcommittee's report, and he hoped the work done by the subcommittee would continue to be a matter of discussion at meetings of the full Committee and of the executive committee.

Thereupon, without objection, Chairman Martin's report was accepted and it was agreed that the ad hoc subcommittee be discharged.

Mr. Robertson then made a statement substantially as follows:

The recent "swap" transactions were not of great quantitative importance, but they do serve to point up the fundamental and recurring question of the appropriate role of our open market operations.

As I understood it, one of the chief purposes of our action at the September meeting was to effectuate further the principle which permeated the ad hoc subcommittee report and underlay the policy decisions of this Committee throughout 1953 - that our intervention in the market should be solely for the objective of providing or absorbing reserves in accordance with the needs of the economy.

There may be circumstances in which our intervention elsewhere than in the shortest-term sector of the market might have beneficial effects from the point of view of debt management, without having any material relation to monetary and credit policy. All of us have given our best thought to this problem, and I for one have concluded that the possible advantages of participating in all sectors of the Government securities market, with a variety of objectives, are outweighed by the benefits of a strictly limited participation. The chief of these benefits, as I see them, are:

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- (1) The likelihood of increased effectiveness of market action designed to effectuate general credit policy when that action is not impeded and its objectives are not obscured by the pursuit of other objectives;
- (2) The development of greater depth, breadth, and resiliency in the Government securities market, as dealers and others become certain, as months go by, that (in the absence of very unusual conditions) the Open Market Committee's transactions will be solely in the shortest-term sector.

The ad hoc subcommittee did a thorough and objective job, and its reasoning and conclusions, together with our discussions of the matter, have convinced me that our wisest course is a policy of rigorous self-limitation along the lines I have described. Our job is to supply reserves and withdraw reserves in order to contribute to the maintenance of an economy that is both stable and highly productive. In ordinary circumstances, the way to accomplish this efficiently, without weakening the fiber of the Government securities market and without tinkering with problems of debt management that are not our responsibility, is to confine ourselves (apart from repurchase transactions) to selling securities in the shortest-term sector when we believe reserves should be absorbed and buying such securities when we believe additional reserves should be supplied. This will enable us not only to pursue single-mindedly our most vital duty of keeping reserves as close as possible to the optimum level, but at the same time to contribute to the strength of the market by enabling dealers and investors to make decisions and take positions with a minimum of worry about a massive but largely imponderable "X" factor - i.e., the effect of transactions on behalf of the overpowering portfolio of the Federal Reserve System.

Needless to say, this policy would bar such "swap" transactions as took place during the past month, since their purpose and effect were not the supply or absorption of reserves.

In view of the fears expressed in September that our action in this matter might be regarded as immutable - written in tablets of stone, as Mr. Sproul said - it is appropriate to reiterate that what I propose is no more than a statement of the present policy of the Committee, always subject to modification at any time when experience with the policy or changed conditions call for modification.

Therefore, I move that the Federal Open Market Committee adopt the following policy, to be followed until such time as it may be superseded or modified by further action of the Committee:

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Transactions for the System account in the open market shall be entered into solely for the purpose of providing or absorbing reserves (except in the correction of disorderly markets), and shall not include offsetting purchases and sales of securities for the purpose of altering the maturity pattern of the System's portfolio.

Mr. Mills stated that he would agree with the proposal that transactions for the System account in the open market shall be entered into solely for the purpose of providing or absorbing reserves (except in the correction of disorderly markets). However, it was his impression, he said, that the ad hoc subcommittee's study of swaps and recommendation for their elimination had reference only to occasions of Treasury refundings. It was his belief that the swap transactions currently undertaken had especial characteristics having to do with corporate financing in the market that were not comprehended by the ad hoc subcommittee's finding against such actions. It was his conclusion that the present experience with swap transactions had served the useful purpose of clearly demonstrating their inadvisability under all foreseeable circumstances. He would, therefore, favor the motion proposed by Mr. Robertson.

Mr. Earhart inquired whether there was any objective in the swap operations carried on since the meeting of the executive committee on November 23, 1953 beyond that indicated by the minutes of that meeting, namely, to acquire some additional holdings of bills in order to facilitate operations in the System account in carrying out credit policy.

Mr. Rouse stated that at the meeting of the executive committee on November 23 there was some discussion of the possibility of withdrawing

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reserves from the market in January and the suggestion for authorizing swaps was for the purpose of increasing holdings of January bills in order to facilitate the withdrawing of reserves in January if that seemed desirable under the Committee's credit policy. He stated that the proposal was not for the purpose of changing the maturity of the portfolio of the System account in any other sense. He further noted that the System account was passive in the operation. It had simply responded to offers from the market.

Chairman Martin noted that the executive committee made the decision to authorize the swaps at its meeting on November 23 and that the Manager of the System Account had engaged in the swap transactions referred to pursuant to the action taken by the executive committee at the time. He stated that while Mr. Robertson had raised the question of validity of that authorization, he (Chairman Martin) was inclined to think that the executive committee had authority to authorize such transactions and that it acted within its authority at the November 23 meeting. However, since a question as to the validity of the action had been raised, Chairman Martin felt it would be preferable to have the action confirmed by the full Committee at this meeting.

Chairman Martin went on to say that in approaching this problem he felt the full Committee should be very careful not to find itself in the position of being "doctrinaire" about the matter. He did not feel that the swaps made in the account during the period since November 23 had

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seriously impaired the market although as a matter of principle, generally speaking, he felt that the position suggested by Mr. Robertson in his motion would be a sound position in the light of the general philosophy under which the Committee had been working for some time.

Mr. Robertson emphasized that he was not contending that the action of the executive committee was clearly invalid legally; he was merely saying its validity was questionable and that it would be desirable to clarify in the record the authority for the action that had been taken as well as to indicate what the full Committee felt should be the authority of the executive committee in this connection hereafter.

Mr. Sproul noted that he was not present at the meeting of the executive committee on November 23, and he then made a statement substantially as follows:

1. Governor Robertson's motion suggests that the sole purpose of open market operations is to put reserve funds into the market and to take them out. It can properly be said that this is the primary function of open market operations, but to say it is the sole function is much too narrow an interpretation; much narrower than saying that the sole purpose is to effectuate the objectives of monetary and credit policy. And it also denies secondary functions, one of which the Committee has formally recognized in connection with debt management.
2. The motion goes on from this sweeping but narrow generalization to a prohibition of "swaps" by the open market account. Recent swaps approved by executive committee in the short-term sector of market were an appropriate use of System portfolio - they helped the banks and particularly others to readjust their short maturities as they desired, and increased the System's holdings of January bills which we may want to use as a weapon of credit policy. That it may have prevented some decline in yields of other short securities and some rise in bill yields is

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no particular concern of ours in the existing situation, and no real interference with market flexibility.

3. It is now held or charged or suggested that there was some breach of principle in this action. This is the doctrine of the unbreachable principle in its most extreme form.
4. For my part I see no breach of principle in this action but if there were I would be for it.
5. As I said in my recent letter to members of the Committee, I see no compelling reason permanently to proscribe swaps by the System Account.
6. The purpose of such swaps in their broader meaning would not be to operate against a market trend but to steady a market groping for the trend, and to bring about desirable adjustments in the Account portfolio, in terms of credit policy.
7. With the present enormous volume (and variety) of Government securities, both actually and in relation to all other debt instruments, and with the whole private security market basing itself, in part, on the Government market, I think we may be asking too much of that market at all times and in all circumstances to make prompt adjustments to sudden changes in credit or other conditions. The advantages of allowing the large System portfolio to assist in this process, at times, seem to me to outweigh the disadvantages. We would still have plenty of flexibility in the market and plenty of room for private arbitrage, on the part of the great majority of those interested in and concerned with the Government security market. Only a very few most agile operators might feel their style might be cramped. I doubt if even they would be seriously hindered in their proper pursuit of profits in the Government security market - but in any case open market policy shouldn't be determined by their views or assumed needs for "freedom" in the market.

In response to a question from Mr. Leach as to exactly what is undesirable about swaps, except that some in the market may object to them, Mr. Mills said that he had reached the conclusion from watching the

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operations of the System account recently that the swaps that had taken place had clouded the pattern of the Government securities market. It was his view that dealers in Government securities were very alert to every influence injected into the market and that where that influence was in the form of entrance by the System open market account in a manner which was not clearly discernible in its objectives, the action might cause confusion among Government securities dealers in reaching their judgments. On the whole, Mr. Mills felt that the disadvantages of the swaps outweighed the possible benefits from such operations.

In response to a question by Mr. Rouse as to what objectionable effects had been observable in the market recently, Mr. Mills stated that the effects of the recent swaps had been only nominal. However, it was his view that to inject into the market any extraneous influence that was apart from the free market concept would result in throwing a haze over the market. This could be easily avoided, he said, by refraining from swaps which might militate against the depth, breadth, and resiliency sought in the market.

Mr. Rouse responded that there had been no discernible effect on dealer positions or on the willingness of dealers to take positions.

While there may have been no observable effect on the position of dealers, Mr. Mills said he felt that the recent swaps had given the dealer fraternity some indication that the System open market account may, on occasion, enter the market for purposes other than providing or

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absorbing reserves or correcting disorderly markets, that this would cause uncertainty, and that the sooner such uncertainties could be disabused, the better.

Mr. Szymczak stated that while he attended the meeting of the executive committee on November 23, he withdrew from the room before the action was taken authorizing swaps. Had he been present at that time, he said, he would have indicated disagreement with the proposal for such swaps. The small amount of bills acquired in the recent operation, which admittedly had had only nominal effects in the market, did not increase the System's holdings of bills sufficiently to help significantly in carrying out credit policy; and if the swaps had been in sufficient volume to have facilitated carrying out credit policy, the swaps would have caused a disturbance in the market. Mr. Szymczak felt there was no need for the question to have come before the full Committee, that it would have been sufficient for the executive committee at its meeting today to have indicated that the swaps that had been authorized by it on November 23 should be discontinued.

Mr. Vardaman felt that the question was one to be determined by the full Committee rather than the executive committee since, in his judgment, engaging in swaps amounted to market manipulation rather than operations to carry out credit policy, and the authority for such activities should definitely be removed from the executive committee. If at any time the full Committee felt it desirable to engage in swaps, it could authorize such transactions.

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At Mr. Johns' request, Mr. Robertson reread his motion, following which Mr. Johns expressed the view that the first clause of the proposed resolution, i.e., "transactions for the System account in the open market shall be entered into solely for the purpose of providing or absorbing reserves (except in the correction of disorderly markets)", would be repetitive of the position that was implicit in the Committee's action last March in agreeing that "it is not now the policy of the Committee to support any pattern of prices and yields in the Government securities market and intervention in the Government securities market is solely to effectuate the objectives of monetary and credit policy (including correction of disorderly markets)". While the wording was slightly different, Mr. Johns felt that the effect was the same.

Mr. Robertson stated that he thought the action approved in March was designed to achieve the same end, but obviously it had failed to do so as evidenced by the recent use of "swaps"; the wording of his motion was intended to make specific and thus to clarify the intention of the full Committee so that there could be no misunderstanding in the future.

Mr. Johns said that he was present and serving on the executive committee at the meeting on November 23 when it authorized the swaps under discussion, that he would be entirely willing at this time to reverse that action and withdraw the authority. He was doubtful about the need for Mr. Robertson's motion, however, his feeling being that the general policy was pretty well understood and that the proposed resolution might be confusing rather than clarifying.

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Mr. Robertson stated that he felt it preferable to have the full Committee's intentions explicitly stated in the minutes rather than to leave the matter to a general "understanding".

Mr. Mills questioned whether the ad hoc subcommittee or the full Committee had ever considered prohibiting swap arrangements except during periods of Treasury refundings. It was his view that if the full Committee desired to prohibit swaps, the question of authority could only be settled by a motion such as that proposed by Mr. Robertson.

During a further discussion of this question, Mr. Erickson stated that he felt the action taken by the executive committee on November 23 in authorizing swaps was fully within its authority, that under the circumstances he felt it was appropriate to authorize the management of the account to engage in swaps for the purpose indicated, that he still felt that under the same set of circumstances at a future time similar authority should be given, and that he therefore would oppose a motion such as that proposed by Mr. Robertson.

Chairman Martin said that unquestionably the over-all concept embodied in the proposed prohibition of swaps permeated the ad hoc subcommittee report; if that concept would be clarified without having such clarification preclude reopening the question at any time, he felt it wholly appropriate to vote on Mr. Robertson's motion.

Mr. Sproul responded that while the theory embodied in the motion probably may have permeated the whole ad hoc subcommittee report, the whole

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ad hoc subcommittee report was never accepted by the Federal Open Market Committee in toto. The suggested resolution would go beyond what was set forth in the ad hoc subcommittee report. In Mr. Sproul's view, the emphasis in open market operations should be on putting reserves into or taking them out of the market, and the ad hoc subcommittee report indicated that to be the primary responsibility of the Committee, but the entire experience of the Committee's operations indicated that there might be times when money market factors (and therefore credit policy) suggested operations which were not solely for the purpose of putting in or taking out reserves. Mr. Sproul felt that if the Committee adopted the proposed prohibition, it would be moving further into a situation of freezing itself into a position from which it would be difficult to extricate itself; its adoption would be an attempt to put the Open Market Committee on record in such a way that the idea of resiliency or flexibility in its policy formation would almost disappear.

Mr. Erickson stated that he would dislike having the record show a formal motion approving Governor Robertson's proposal and suggested that the concept might be indicated satisfactorily by having the minutes of this meeting show that it was the sense of the Committee that operations ordinarily should avoid swaps.

Chairman Martin stated that there certainly was no intention on his part or on the part of the ad hoc subcommittee of denying the validity of flexibility of operations. He recognized that it could be argued that either the position taken by the ad hoc subcommittee or the position

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suggested by Mr. Sproul would work against flexibility. It seemed to him, however, that it was more appropriate to develop a philosophy and make exceptions to that philosophy, rather than to take the view that there should be no philosophy.

Mr. Sproul thought that a philosophy had been developed in general terms by the Committee but that Mr. Robertson's motion tended to push that philosophy into a corner out of which the emergence of a flexible policy would become more and more difficult.

Chairman Martin stated that it should be clearly understood by all members of the Committee that, in the event Mr. Robertson's motion should be voted on and carried, the Committee should have no hesitancy in reversing the action in the event circumstances arose which made that seem to be desirable. This could be done at any time by calling a meeting of the full Committee or, in the event of need, by telephone.

During a further discussion of this question, Mr. Sproul again expressed the view that step by step the Committee was building a pattern of very limited flexibility or none at all.

Mr. Earhart suggested that it might be more disturbing to the Government securities market if, in January, the System account were to make outright sales of securities in order to contract the supply of reserves, than to have swaps such as were authorized by the executive committee on November 23 take place during December.

Chairman Martin responded that it was always a matter of judgment, of balancing between a philosophy of a free market and the degree to which

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the Federal Open Market Committee assumed responsibility for the market. In the longer run, what would produce depth, breadth, and resiliency in the market? His own views were at the opposite pole from those expressed by Mr. Sproul, he said, but he recognized that judgments might differ on what would produce the kind of market that was being discussed.

Mr. Leach stated that if he were a member of the Committee he would vote against Mr. Robertson's motion, assuming that the action that would be taken would have to be included in the record of policy actions to be published in accordance with Section 10 of the Federal Reserve Act. His disposition was not to take formal actions of this sort which had to be made a matter of public record.

Chairman Martin noted that the action of the Committee in June in reversing by a five to four vote the action that had been taken by the full Committee in March with respect to confining operations to short-term securities and to refraining from certain operations during periods of Treasury financings was one which would have to go into the policy record. He did not feel that the concept of a free market was one on which the members of the Committee could refuse to take a definite stand.

Mr. Sproul then moved that, without accepting in any way the idea of a perpetual policy such as was suggested by Mr. Robertson's resolution, that motion be amended to provide that it would be effective "until the next meeting of the Federal Open Market Committee".

Mr. Sproul stated that his reason for moving to amend Mr. Robertson's motion was that the whole temper of the discussion of that motion

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as well as of Mr. Mills' motion which was approved at the meeting on September 24, 1953 had been to the effect that the actions proposed were always subject to review. While he assumed that all members of the Committee would agree that the action proposed by Mr. Robertson would be effective only until the next meeting, Mr. Sproul felt that it was important enough to warrant having this point clearly stated so that the Committee would not slide into the position of having frozen policy indefinitely.

Mr. Robertson stated that he would prefer not to have his resolution amended as proposed by Mr. Sproul inasmuch as such an amendment would mean that the resolution automatically became ineffective after the next meeting of the Committee unless positive action were then taken to renew it.

Mr. Williams then suggested that the executive committee would have a pretty clear indication of what the full Committee had in mind if, in Mr. Robertson's motion, the word "primarily" were substituted for the word "solely" so that the affected part of the motion would read "..... transactions for the System account in the open market shall be entered into primarily for the purpose of providing or absorbing reserves....."

Mr. Robertson replied that he would be opposed to the change recommended by Mr. Williams since there was no clear understanding of what would fall outside the realm of "primarily". Thus, such a change would, in effect, defeat the purpose of his motion which was intended to draw a

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dividing line which, without further interpretation, would be clearly understood by everyone concerned.

Chairman Martin stated that, for the reasons given by Mr. Robertson, he would dislike substitution of the word "primarily" for "solely".

Following a discussion, Mr. Sproul's motion to amend Mr. Robertson's motion was put by the Chair and lost: Messrs. Sproul and Erickson voting "aye" and Messrs. Martin, Evans, Fulton, Johns, Mills, Powell, Robertson, Szymczak, and Vardaman voting "no".

Mr. Robertson's motion, that transactions for the System account in the open market shall be entered into solely for the purpose of providing or absorbing reserves (except in the correction of disorderly markets), and shall not include offsetting purchases and sales of securities for the purpose of altering the maturity pattern of the System's portfolio, was then put by the Chair and carried: Messrs. Martin, Evans, Fulton, Johns, Mills, Powell, Robertson, Szymczak, and Vardaman voting "aye", and Messrs. Sproul and Erickson voting "no".

Mr. Sproul stated that he had another proposal to make which was related to the foregoing discussion. He referred to the action taken by the Committee at its meeting on September 24, 1953 in approving the motion by Mr. Mills that "the Federal Open Market Committee take the position that operations for the System account be confined to short-term securities (except in the correction of disorderly markets) and that during a period of Treasury financing there be no purchases of (1) maturing issues for which an exchange is being offered, (2) when-issued securities, or (3) outstanding issues of comparable maturity to those being offered for exchange; and that

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these policies be followed until such time as they may be superseded or modified by further action of the Federal Open Market Committee".

Mr. Sproul then moved that the last clause of the foregoing action taken at the meeting on September 24, 1953 be amended to read "and that these policies be followed until the next meeting of the Federal Open Market Committee."

In commenting upon this motion Mr. Sproul stated that, in proposing the amendment, he was in no way altering his opposition to the general purport of the whole action approved by the full Committee on September 24, 1953. He felt, however, that the proposed language would correctly reflect the sense of the meeting on September 24, that is, that the action would be subject to review at the next meeting of the Committee. He preferred the suggested wording, he said, so that everyone would know that the action taken did not represent a permanent policy.

During the discussion that followed, Mr. Szymczak expressed the view that those who might not vote to approve Mr. Sproul's motion would not necessarily have any objection to considering the question at the next or any other meeting of the Committee.

Mr. Mills raised the question whether in the opinion of the Counsel for the Committee modification of the action taken at the meeting on September 24 by including a specific time limitation such as suggested by Mr. Sproul's motion was necessary to preserve the legal freedom of action for the Committee's members subsequently to alter their views.

Mr. Vest stated that from the legal standpoint it was clear that any member of the Committee had the right at any meeting to bring up any

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subject of the type under discussion for consideration; whether the specific provision suggested by Mr. Sproul was included in the resolution or not, this right was always there as a legal matter and could not be taken away by action of the Committee.

Mr. Erickson stated that he would vote to approve Mr. Sproul's motion since it represented the position which he had felt all along existed and since it would not alter the views he held in voting to approve Mr. Mills' resolution at the meeting on September 24, 1953.

Thereupon, Mr. Sproul's motion was put by the Chair and lost: Messrs. Sproul and Erickson voting "aye" and Messrs. Martin, Evans, Fulton, Johns, Mills, Powell, Robertson, Szymczak, and Vardaman voting "no".

Mr. Robertson stated that so long as the question of the action taken by the Committee at the meeting on September 24 had been raised, he would suggest that the wording of the motion be clarified by inserting the words "in the open market" following "System account" so as to make it clear that the action applied only to transactions in the open market and not to transactions with the Treasury.

This suggestion was discussed briefly and it was agreed unanimously that, as a matter of clarification of the subject action taken at the meeting on September 24, 1953, the words "in the open market" be inserted following the words "System account".

Secretary's note: With this change, the action would read as follows:

"Mr. Mills then moved that the Federal Open Market Committee take the position that

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operations for the System account in the open market be confined to short-term securities (except in the correction of disorderly markets) and that during a period of Treasury financing there be no purchases of (1) maturing issues for which an exchange is being offered, (2) when-issued securities, or (3) outstanding issues of comparable maturity to those being offered for exchange; and that these policies be followed until such time as they may be superseded or modified by further action of the Federal Open Market Committee."

Mr. Vardaman withdrew from the meeting at this point.

Chairman Martin then called upon Mr. Thomas who commented briefly on the outlook for the reserve position of banks after the turn of the year, particularly the effects of the return flow of currency from circulation following the holiday shopping season and the easing influence such return flow would have on the money market. (A Staff memorandum on The Outlook for Treasury Cash Requirements and Bank Reserves had been distributed to the members of the Committee under date of December 11, 1953.) Mr. Thomas raised the question whether the Committee would wish to withdraw funds from the market during January as a means of avoiding a large volume of free reserves (excess reserves less discounts and advances) during that period. It was his view that, assuming that any additional reserves supplied by open market operations between December 10 and the year-end were made available through the repurchase facility and assuming further that repurchase contracts were fully repaid early in January, the System would need to mature or sell about \$500 million of Treasury bills in January if free reserves were to average about \$100 million by late January.

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Chairman Martin suggested that consideration be given at this point to the memorandum from Messrs. Riefler and Thomas dated December 9, 1953, to which he had referred earlier in this meeting. While he did not believe the Committee was prepared to make changes at this time, he felt discussion of the subject was desirable since questions had been raised regarding the recent action of the manager of the System open market account in reducing the effective rate on repurchase agreements to 1-3/4 per cent, a level below that of the discount rate (2 per cent). He noted that there had also been a question whether repurchase facilities should be extended to member banks rather than only to non-bank dealers in Government securities. With respect to the relationship between the discount rate and the repurchase rate, it was Chairman Martin's view that an educational process had been taking place in the market and that action to lower the discount rate in December and put it back up in January would be widely misinterpreted in the business community.

Chairman Martin went on to say that the action in reducing the repurchase rate was taken under the authority given to the manager of the System account by the full Committee, after the manager of the account had discussed the proposed action with him (Chairman Martin).

Mr. Sproul then made a statement substantially as follows:

1. I think a repurchase rate lower than the discount rate is peculiarly adopted to relieving temporary situations in the money market and can effectively and most appropriately be carried out by making it available to Government security dealers, other than banks.
2. We have an example in the recent situation. As Governor Mills pointed out at the last meeting of the executive committee, we

had a relatively easy reserve position in most of the country and relative tightness in New York. It was a money market phenomenon of temporary character. Our job was to smooth it out, without actual or apparent major or significant changes in general credit policy. A reduction in the repurchase rate and an increased use of repurchase facilities avoided a temporary undue run-up of rates and a temporary undue tightening of credit due to increased bank borrowing, and also avoided the substantially more permanent commitment of a reduction in the discount rate, and the slightly more permanent commitment of larger outright purchases of Government securities. It emphasized the money market aspect of the situation as distinguished from the overall business and credit aspect.

3. Used in this way to meet temporary situations, which I think is the way it should be used, I see no need to extend the repurchase privilege to dealer banks nor to all banks. The banks are able to make their necessary adjustments in large part through the Government security market by virtue of the repurchase facility afforded to the dealers, and without resort to the amount of borrowing which would otherwise be necessary.

4. To expand the privilege by making it available to dealer banks, in addition to being unnecessary to make the machinery work, would seem to me to run counter to a fundamental tenet of the Federal Reserve Act that the affairs of each Federal Reserve Bank will be administered fairly and impartially without discrimination in favor of or against any member bank or banks.

5. To try to overcome this difficulty by making the facility available to all member banks would seem to me to lead us into an error to correct an error which doesn't exist. It would be, in effect, the establishment of a preferential borrowing or discount rate. And one thing I think we have learned is that no matter how you slice it, the preferential rate becomes the effective discount rate, at least for the banks that know how to use it. I don't think we want to get back into that situation. Repurchase agreements have been and can be used effectively as an instrument of monetary policy geared specifically to meet temporary situations in the money market--of which the Treasury short term market is now the core. There is a clear difference between the repurchase rate in its restricted use and the discount rate in its general use, and I don't think that distinction should be blurred.

If the repurchase rate didn't become a preferential rate, it would be because most banks were not familiar with it, and then we would be right back where we started, with a special facility for a few money market banks.

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In response to a question from Chairman Martin, Mr. Sproul indicated that he would contemplate that the existing rate on repurchase agreements would be kept until about the end of this year; the usefulness of the present $1\frac{3}{4}$ per cent rate on repurchase agreements would be ended with the return flow of funds after the turn of the year when repurchase contracts would be repaid.

There followed a general discussion of the use of repurchase agreements and of the question whether the rate on such agreements should be set at a level below the discount rate of the Federal Reserve Banks. During this discussion, Chairman Martin stated that he was in complete agreement with the views expressed by Mr. Sproul regarding repurchase agreements. He felt they represented an appropriate device in the money market which could be used from time to time in helping to accomplish the objectives of credit policy, and he noted that they had been used since the early 1920's, the Board having then authorized the Federal Reserve Banks to engage in such transactions.

Messrs. Robertson, Bryan, and Johns expressed some doubts as to the appropriateness of present arrangements for repurchase agreements but were not prepared to suggest changes in the procedure for their use at this time.

Mr. Mills suggested that, entirely apart from the procedure for using repurchase agreements, he sensed a tendency to rely unduly on such facilities as a means of supplying reserves over the coming year-end period. He felt System policy should be careful not to exclude outright purchases of

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securities in the event repurchase agreements did not meet the needs of the market for reserves.

Mr. Sproul stated that, while the question of the credit policy to be pursued in coming weeks had not yet been acted on by the Committee, he would agree that if conditions developed where repurchase agreements were not taking care of the situation in accordance with the Committee's credit policy, outright purchases of securities should not be excluded.

The discussion then turned to the credit policy to be followed during coming weeks in the light of the economic review presented earlier in the meeting and of the review Mr. Thomas had given of the projections for bank reserve positions, particularly through the month of January. Chairman Martin noted that the Committee had been pursuing a general policy of "active ease" in the money market, which meant that reserves would be supplied to the market to meet seasonal and growth needs of the economy. He inquired whether, in terms of the foregoing discussion, any of the members of the Committee felt there should be a modification of the Committee's existing policy.

This question was considered and there was unanimous agreement that the over-all credit policy should continue along the lines that had been pursued recently with, however, more emphasis on a program of actively maintaining a condition of ease in the money market.

In this connection there was also a discussion of the possible desirability of a reduction in the discount rate of the Federal Reserve Banks as a means of helping to carry out the Committee's stated policy of actively

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maintaining a condition of ease in the money market.

Mr. Johns stated reasons why he felt a reduction in the discount rate might be considered at this time, emphasizing that such a reduction need not be thought of as something of a very temporary nature to be followed by an increase soon after the first of the year; it was Mr. Johns' thought that a reduced discount rate at this time might be a desirable indication of flexibility.

Several of the other members of the Committee and Presidents of Federal Reserve Banks who were not members of the Committee questioned the desirability of a reduction in the discount rate at this time.

Chairman Martin expressed the view that a reduction in the discount rate at present might "muddy the stream" in view of the fact that the Committee had already started on a program of meeting year-end credit demands by use of repurchase agreements. As to the business situation, he noted differences of opinion on how serious the current readjustment might be and suggested that on the whole it might be wiser to avoid changing the discount rate at the present time.

Mr. Sproul agreed with these comments, adding the view that the thoughts expressed regarding the discount rate in no way indicated a feeling on the part of the members of the Committee that its credit policy should in any sense be one of restraint during the period immediately ahead.

The meeting recessed at 1:10 p.m. and reconvened at 2:00 p.m. with the same attendance as at the close of the morning session.

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During a discussion of the directive to be issued, it was suggested that the clause in the existing directive which had provided that the executive committee should arrange for transactions for the System open market account with a view, among other things, "to avoiding deflationary tendencies" should be changed in keeping with the decision at the morning session that the over-all objective of credit policy should be one of actively maintaining a condition of ease in the money market.

There was also a discussion of the purpose of clause (d) of the directive which authorized that transactions be with a view "to the practical administration of the account". Mr. Vest said that it was difficult to state precisely what was authorized by this clause but that it gave a certain amount of leeway for incidental transactions in the account which were necessary to carry out effectively and appropriately the policies otherwise prescribed by the Committee, within the limitations established under the general policy or other directives adopted by the Committee. Mr. Vest noted that the clause in its present form or in a similar form had been used in virtually all directives of the Federal Open Market Committee and of the executive committee since the Committee was reorganized pursuant to the Banking Act of 1935.

After some discussion, Chairman Martin suggested that the clause be retained in the directive to be issued at this meeting but that its purpose be reviewed before the next meeting, and there was unanimous agreement with this suggestion.

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Following a further discussion, during which it was stated that no change in the limitations contained in the directive was necessary, upon motion duly made and seconded, unanimous approval was given to a directive in the following form:

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 (a) to relating the supply of funds in the market to the needs of commerce and business, (b) to promoting growth and stability in the economy by actively maintaining a condition of ease in the money market, (c) to correcting a disorderly situation in the Government securities market, and (d) 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.

It was agreed that the next meeting of the Committee would be held during the week beginning March 1, 1954.

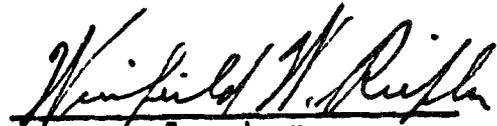
Mr. Robertson stated that, since the ad hoc subcommittee was being discharged, he would not wish to have this meeting adjourn without first saying that he felt the subcommittee was entitled to the commendation of

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the entire Federal Open Market Committee. He felt that the job the subcommittee had done was of great benefit to the System, not only because of the specific suggestions it had made, but even more particularly because of the general interest it had stimulated among the members of the Federal Open Market Committee in open market operations. Mr. Robertson added the comment that he felt especially indebted to the subcommittee for the work it had done.

Thereupon the meeting adjourned at 2:15 p.m.


Secretary