

A meeting of the executive committee of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System in Washington on Wednesday, June 23, 1948, at 10:30 a.m.

PRESENT: Mr. McCabe, Chairman
Mr. Sproul, Vice Chairman
Mr. Eccles
Mr. Draper (alternate for Mr. Szymczak)
Mr. Young (alternate for Mr. Williams)

Mr. Morrill, Secretary
Mr. Carpenter, Assistant Secretary
Mr. Vest, General Counsel
Mr. Thomas, Economist
Mr. Thurston, Assistant to the Board
Mr. Miller, Assistant Vice President,
Federal Reserve Bank of New York
Mr. Smith, Economist, Government Finance
Section, Division of Research and
Statistics, Board of Governors

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the executive committee held on May 20, 1948, were approved.

Upon motion duly made and seconded, and by unanimous vote, the actions of the members of the executive committee on May 28 and June 1, 1948, increasing from \$750 million to \$1 billion and from \$1 billion to \$1,250 million, respectively, the limitation contained in the first paragraph of the direction issued at the last meeting of the committee to the Federal Reserve Bank of New York to execute transactions for the System open market account, were approved.

Thereupon, Mr. Miller presented and discussed a memorandum reviewing the market for United States Government securities and

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transactions in the System account for the period May 20 to June 21, 1948, inclusive. He also submitted a supplementary report covering transactions in the System account on June 22, 1948. Copies of these reports have been placed in the files of the Federal Open Market Committee.

There was a discussion of recent market developments, including (1) the effect on the market of the increase in reserve requirements of member banks in central reserve cities which became effective on June 11, 1948, and (2) the special offering of series F and G savings bonds to institutional investors during the period July 1 to July 15, 1948.

In connection with the latter action Mr. Sproul stated that when the representatives of the committee went to the Treasury in April they recommended against any extensive increase in the limit on series F and G bonds and that that recommendation was renewed during meetings with representatives of the Treasury during May at which time the representatives of the committee were informed that some liberalization was being considered. Mr. Sproul, in this connection, referred to the fact that the letter sent to the Treasury on June 2, 1948, recommended that the limit on F and G bonds for pension fund investment only be increased to \$200,000 or \$250,000.

Chairman McCabe observed that market quotations on long-term Treasury bonds were substantially above the System support prices

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and inquired why it had not been possible to sell more of these issues from the System account.

Mr. Miller responded that the rise in prices largely reflected psychological influences, but that there was no real strength in the market, and that increased offerings would probably drive prices down. He also stated that the dealers had a position of about \$130 million in restricted issues and that, if the System should undertake to sell from its holdings during a period when the market lacked fundamental strength, the dealers, fearing a substantial market decline, would immediately undertake to sell their holdings which would certainly drive prices down which made it undesirable to attempt any large amount of sales from the System account.

Mr. Eccles stated that the System was faced with the alternative of actually taking the place of the dealers or permitting them to operate in the manner in which they had operated in recent years, that the System stood in the position of the residual buyer or seller for the purpose of maintaining stability in the market, and that if the System now undertook to sell any substantial amount of its holdings of long-term bonds it would force the market down to the support prices so that the market would be pegged on both the up and down side.

Chairman McCabe pressed his question, inquiring as to the reality of the quotations and as to the circumstances under which the System would be able to sell long-term securities from the

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from the System account, and there was a discussion of the decision reached at the meeting of the full Committee on May 20 that, if the bond market continued strong, the Federal Reserve Bank of New York would sell bonds from the System account in such amounts as to resist a rise in prices, it being understood that selling would be accelerated as prices went up without at any time stopping the rise.

Mr. Eccles stated that if, during the early part of last year when there was a strong demand for long-term issues, the System had held its present portfolio of these issues, a substantial amount of them could have been disposed of in the market as a means of counteracting the upward movement, but that inasmuch as the System held practically none of these maturities, the Treasury had sold in the neighborhood of \$2 billion from its trust accounts for that purpose and, in addition, offered a special issue of 2 1/2 per cent investment series A bonds to aid in satisfying the demand for long terms. If another situation of that kind should arise, he said, it would be possible to dispose of a substantial amount of the System's long-term holdings.

In response to Chairman McCabe's question Mr. Miller stated that since the last meeting there was no real demand in the market for Treasury bonds, and that in the neighborhood of 90 per cent of market activity in those issues had been swap transactions rather than outright purchases or sales of securities.

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In a further discussion, excerpts were read from the minutes of the meetings of the executive committee and the Federal Open Market Committee on May 20 with respect to the sale of long-term securities from the System account and Mr. Sproul stated that the Federal Reserve Bank of New York had been operating in accordance with the agreement reached at the meeting of the full Committee.

At the conclusion of the discussion, upon motion duly made and seconded and by unanimous vote, the transactions in the System account, as reported to the members of the executive committee, for the period May 20 to June 22, 1948, inclusive, were approved, ratified, and confirmed.

Upon motion duly made and seconded, and by unanimous vote, the letter sent to the Secretary of the Treasury under date of June 2, 1948, with respect to a new issue of savings notes and an increase in the annual limit of series F and G bonds, was approved and its transmission to the Treasury was ratified and confirmed.

Mr. Sproul stated that the System account held approximately \$2,300 million of the maturing July certificates, and that, while the most recent estimates of the Treasury cash position indicated that there would be an opportunity for further retirement of marketable debt, it was his opinion that, in view of the weakness of the market for June and July certificates, it would be desirable for the System to replace its entire holdings of the July maturity and to recommend to the Treasury that it retire \$200 million of each of the Treasury bill maturities on July 1 and July 8, 1948.

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In a discussion of Mr. Sproul's suggestion, and of a comment by Mr. Eccles that if calls on war loan accounts were timed to neutralize Treasury operations the actual retirement of Treasury securities would not be important from the standpoint of the money market, Mr. Sproul stated that the retirement would be an indication that the policy was being continued of keeping pressure on the market.

Reference was made to possible changes in the cash position of the Treasury over the next few months and various possible actions were suggested with respect to the retirement of maturing securities.

Mr. Sproul suggested that the recommendation to the Treasury might be that calls on war loan accounts be timed so that Treasury operations would at least exercise a neutral effect so far as bank reserves were concerned, that if a situation should develop in which it was desirable to exert added pressure on the market calls on war loan accounts could be increased, and that in the meantime the Treasury should retire part of the July 1 and July 8 bill maturities with the understanding (1) that the System's holdings of July certificates would be replaced with the new issue, and (2) that further retirement of Federal Reserve held debt would depend upon developments, including the decision made with respect to the refunding of securities maturing in September.

Mr. Thomas inquired if a decision could not be made at this time whether additional pressure on member bank reserves should be applied in July.

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Mr. Sproul responded that the question was one of timing the action; i.e., whether it would be more effective to put pressure on reserves before evidence of a need therefor with the result that the effect of the action might largely be lost, or whether action should be deferred until the need presented itself when there would be a risk that the action that could be taken by the System would not be sufficient to counteract the movement. In his opinion, it was not possible at this time to say when in July or August additional pressure should be applied and that no decision should be made now as to the timing of further action.

After some further discussion, Mr. Sproul's suggested procedure was approved unanimously as a recommendation to be made to the Treasury.

The discussion then turned to the procedure that might be followed to increase the short-term market rate, and Mr. Sproul stated that a further increase in the short-term rate would become more important than otherwise if the Treasury should decide to refund some of the longer term higher rate securities which would mature over the next two or three years into securities bearing a higher rate than certificates. He felt that because of the large volume of such maturities the Treasury might want to consider that possibility. He felt also that, regardless of the decision on that point, it was important that the short-term rate be increased and that there be early discussions with representatives of the Treasury for the purpose of working out a procedure for allowing the short-term rate to

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go up in the market preparatory to completing the September financing at a 1 1/4 per cent rate.

Chairman McCabe expressed the opinion that the representatives of the Federal Open Market Committee should be prepared to make a strong presentation of its position that action should be taken and he asked for discussion of the procedure that might be followed in permitting the short-term market rates to rise.

There was a discussion of whether it would be more effective to allow the rate to increase gradually or whether the change should be effected in one step and Mr. Miller expressed the opinion that if an indication were given that the support prices were to be lowered it would be known that the next point would be 1 1/4 per cent, and that, therefore, the System would have to purchase more securities if the increase was gradual than if the change were made in one step.

During the discussion Chairman McCabe suggested that the Treasury be advised that the committee had reviewed the credit situation and questions with respect to Treasury financing and debt management, that the committee was concerned about the System's responsibilities for the credit situation, and that it felt that action should be taken to increase the short-term market rate by permitting the bill rate to rise, and the price of certificates to adjust to the bill rate, until the certificate rate had reached 1 1/4 per cent, the timing of the action to be subject to decision in the light of developments prior to the September financing.

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It was the consensus of the members present that if, after the matter was discussed with the Treasury, the Treasury was unwilling to accept such a recommendation, another meeting of the executive committee should be held to ascertain whether it would discuss the matter further with the Treasury or call a meeting of the full Committee.

Mr. Eccles outlined reasons that might be advanced to the Treasury for increasing the short-term rate, and he discussed the problem that would be presented if the Treasury should wish to refund some of the long-term issues maturing over the next two or three years with issues maturing some time after 1952.

At the conclusion of the discussion, it was agreed unanimously that Chairman McCabe should arrange for a conference with representatives of the Treasury during the latter part of the week of July 5 or the early part of the week of July 19, that a draft of memorandum should be prepared to be taken to the Treasury at that time, that the draft should be submitted to the members of the committee for comment before submission to the Treasury, and that in the meantime a letter should be sent to the Treasury which, after referring to the contemplated meeting with the representatives of the Treasury for a discussion of the longer term aspects of some of the problems with respect to debt management, would recommend that the Treasury retire \$400 million of bills maturing in July and that Treasury calls on war loan accounts be timed so that Treasury operations would not result in an increase in bank reserves.

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It was also agreed that the memorandum to be presented at the conference with Treasury representatives should renew the System's recommendation that a new issue of savings notes be offered with a new scale of rates.

Following the discussion of authority to be granted to the Federal Reserve Bank of New York to execute transactions for the System account, it was agreed that a renewal of the direction issued at the last meeting of the committee would be adequate to meet the situation pending another meeting.

Thereupon, upon motion duly made and seconded, the executive committee voted unanimously to direct the Federal Reserve Bank of New York until otherwise directed by the executive committee:

(1) To make such purchases, sales, or exchanges (including replacement of maturing securities and allowing maturities to run off without replacement) for the System account, either in the open market or directly from, to, or with the Treasury, as may be necessary, in the light of the general credit situation of the country, for the practical administration of the account, for the maintenance of stable and orderly conditions in the Government security market, and for the purpose of relating the supply of funds in the market to the needs of commerce and business; provided that the total amount of securities in the account at the close of this date shall not be increased or decreased by more than \$750,000,000 exclusive of special short-term certificates of indebtedness purchased for the temporary accommodation of the Treasury pursuant to paragraph (2) of this direction;

(2) To purchase direct from the Treasury for the System open market account 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 \$750,000,000.

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In taking this action it was understood that the limitation contained in the direction included commitments for purchases and sales of securities for the System account.

It was the consensus of the members present that the date for the next meeting of the executive committee should be fixed following the contemplated conference of representatives of the committee and the Treasury.

Thereupon the meeting adjourned.

Chester Moriel
Secretary.

Approved:

Thomas B. W. Cole
Chairman.