

FORTY-SECOND

# ANNUAL REPORT

*of the*

BOARD OF GOVERNORS OF THE  
FEDERAL RESERVE SYSTEM



COVERING OPERATIONS FOR  
THE YEAR

1955

ments entails no element of price support, and because of the special nature of such agreements, the Committee felt that they ordinarily could appropriately cover Treasury securities which otherwise would not be bought or sold under the Committee's general policy of effecting transactions only in short-term securities and avoiding purchases of securities involved in a Treasury financing.

Mr. Sproul voted against the statements under "B" and "C" because he continued to be opposed to the assertion by the Committee that it has a responsibility solely with respect to the volume of bank reserves; because he continued to oppose the Committee's renunciation of all or any transactions directly related to security issues involved in Treasury financings, as he believed that such transactions might in some circumstances facilitate, rather than interfere with, the attainment of the System's policy objectives; and because he continued to be opposed to the prohibition against offsetting purchases and sales of Treasury securities for the purpose of altering the maturity pattern of the System's portfolio and the limiting of transactions to short-term securities in all circumstances. In voting against these actions, Mr. Sproul said that he had been encouraged by the public statement contained in Chairman Martin's replies to questions submitted by the Subcommittee on Economic Stabilization of the Joint Committee on the Economic Report in connection with subcommittee hearings on December 7, 1954, that these operating policies are experimental, and by the warning this should convey to the market that there is no promise, expressed or implied, that these policies will always be followed.

May 10, 1955

#### 1. Authority to Effect Transactions in System Account.

The following directive by the Federal Open Market Committee was approved:

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

to the Government securities dealers, through sales to them of additional securities or withholding by banks or other lenders of funds needed by the dealers to carry their positions. The technical arrangements consist of a purchase by the System at an agreed price, subject to a dealer's undertaking to repurchase the same securities at the same price, plus a stipulated rate of interest, on or before a maturity date set by the System. In general, the interest rate has been equivalent to the discount rate of the Federal Reserve Bank of New York, although at times there may be a temporary deviation above or below this rate; the maturity has in practice been limited to 15 days or less; and the price set in the contract is determined by the System in each instance at a nominal margin below the latest-prevailing price in the market for the securities involved.

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 fostering growth and stability in the economy by maintaining conditions in the money market that would avoid the development of unsustainable expansion, (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 billion.

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 billion.

Votes for this action: Messrs. Martin, Chairman, Sproul, Vice Chairman, Balderston, Earhart, Fulton, Irons, Leach, Mills, Robertson, Shepardson, Szymczak, and Vardaman. Votes against this action: none.

This directive was modified from that approved at the meetings on January 11 and March 2, 1955 by changing clause (b) to delete the words "encourage recovery" and to make the clause read "to fostering growth and stability in the economy by maintaining conditions in the money market that would avoid the development of unsustainable expansion."

The Committee noted that during the current or second quarter gross national product was estimated at an annual rate of \$375 billion, nearly \$20 billion above the low of last year and \$5 billion above the mid-1953 peak; that strong expansion in activity was generally continuing abroad; and that in the United States a number of industries were operating at or close to capacity. Supply shortages had appeared in some industrial materials and prices of metals had advanced, although price averages were still generally steady. Business, financial, and consumer confidence was extraordinarily

high. On the other hand, manpower and industrial resources of the United States were generally ample for growth, and a substantial amount of unemployment still existed in some areas. Prices of farm products continued under pressure from surplus supplies and excess capacity. There had been no seasonal contraction of business loans, and rapid expansion of real estate and consumer loans had continued. This further expansion in the volume of credit and evidences of continued speculative pressures in the stock markets had been followed by action of the Board of Governors increasing margin requirements from 60 to 70 per cent, effective April 23, 1955.

In deleting the previous instruction to "encourage recovery" the Committee had in mind that recovery now was an accomplished fact and that credit policy need no longer be directed toward encouraging recovery. Its problem now was to conduct open market operations so as to foster stable growth in line with expanding manpower and industrial resources and at the same time to restrain financial over-commitments and dampen speculative excesses. The Committee noted that since its meeting on March 2, the Board of Governors of the Federal Reserve System had approved an increase of  $\frac{1}{4}$  of 1 per cent in the discount rate at all Federal Reserve Banks, in recognition of current money market conditions and as a means of discouraging undue reliance on the discount facilities of the Reserve Banks. Like the change made in the directive of the Federal Open Market Committee in January, the change approved at this meeting was a further shift in emphasis toward a policy that would discourage undue credit expansion. It meant that the Committee was aiming at a lower level of free reserves of banks, and that consequently credit might cost more and be somewhat less readily available. The Committee was seeking to allow market forces to have their effect within some moderate limits, although it favored efforts to smooth temporary swings in money market conditions and to maintain stability in the market during a period of a Treasury financing.

June 22, 1955

#### 1. Authority to Effect Transactions in System Account.

The following directive from the Federal Open Market Committee to the Federal Reserve Bank of New York was approved:

To make such purchases, sales, or exchanges (including replacement of maturing securities, and allowing maturities to run off without replacement) for the System open market account in the open market or, in the case of maturing securities, by direct exchange with the Treasury, 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 fostering growth and stability in the economy by maintaining conditions in the money market that would avoid the development of unsustainable expansion, and (c) 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 \$1 billion.

To purchase direct from the Treasury for the account of the Federal Reserve Bank of New York (with discretion, in cases where it seems desirable, to issue participations to one or more Federal Reserve Banks) 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 \$500 million;

To sell direct to the Treasury from the System account for gold certificates such amounts of Treasury securities maturing within one year as may be necessary from time to time for the accommodation of the Treasury; provided that the total amount of such securities so sold shall not exceed in the aggregate \$500 million face amount, and such sales shall be made as nearly as may be practicable at the prices currently quoted in the open market.

Votes for this action: Messrs. Martin, Chairman, Sproul, Vice Chairman, Balderston, Earhart, Fulton, Irons, Leach, Mills, Robertson, Shepardson, and Vardaman. Votes against this action: none.

This directive was issued by the Committee to the Federal Reserve Bank of New York as the Bank selected by the Committee to execute transactions for the System open market account because earlier during this meeting the executive committee of the Federal Open Market Committee, to which the full Committee formerly issued its directives, was abolished.

In connection with the issuance of the directive running from the Committee to the Agent Bank, there was eliminated one of the provisions that the full Committee previously had included in its instruction to the executive committee, namely, that in arranging for transactions for the System account the executive committee should do so with a view, among other things, "to correcting a disorderly situation in the Government securities market." That provision had been included in the directive to the executive committee since March of 1953 with the understanding that intervention to correct a disorderly situation in the Government securities market would be initiated