

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 Thursday, February 26, 1948, at 2:30 p.m.

PRESENT: Mr. Eccles, Chairman  
Mr. Sproul, Vice Chairman  
Mr. Davis  
Mr. Draper  
Mr. Vardaman

Mr. Szymczak, Member of the Federal  
Open Market Committee

Mr. Morrill, Secretary  
Mr. Carpenter, Assistant Secretary  
Mr. Vest, General Counsel  
Mr. Thomas, Economist  
Mr. Rouse, Manager of the System Open  
Market Account  
Mr. Thurston, Assistant to the Board  
of Governors  
Mr. Smith, Economist, Government Finance  
Section, Division of Research and  
Statistics, Board of Governors  
Mr. Arthur Willis, Special Assistant,  
Securities Department, Federal Re-  
serve Bank of New York

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

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 January 20 to February 25, 1948, in-  
clusive, were approved, ratified and  
confirmed.

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In accordance with the action taken at the meeting of the executive committee on January 20, 1948, a letter to the Secretary of the Treasury setting forth a suggested program to be followed during the first six months of the calendar year with respect to debt and money market management and Treasury refunding had been prepared and, following approval by the members of the executive committee (Mr. Gidney acting in the absence of Mr. Davis) in the form set forth below, was sent to the Treasury under date of February 5, 1948:

"The executive committee of the Federal Open Market Committee met on January 20 and considered the related questions of credit policy and debt management during the first quarter and the first half of 1948. It is the committee's opinion that Federal Reserve and Treasury debt management policies during the immediate future, and unless and until conditions change, should be determined with a view to placing continuing and persistent restraint upon the expansion of bank credit which is contributing to existing strong inflationary forces. It seems likely that there will be a heavy demand for bank loans from business, from consumers, and from real estate owners during the next few months. Further expansion of bank loans to meet these demands will help to finance the continuance of inflation.

"The existence of a large Treasury surplus in the first quarter of the year is the main weapon available for combating inflation in this area. In the first instance, receipt of taxes by the Treasury in excess of current expenditures will reduce bank deposits and bank reserves. The use of this excess to retire debt held by the Federal Reserve Banks will keep these funds from returning to the commercial banks, as they would if the excess were used to retire securities held by such banks or other investors. Since it is the withdrawal of funds from the market by the Treasury which

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"directly affects bank reserves, the timing of these withdrawals is an important factor in the control program. The timing of the retirement of securities held by the Federal Reserve Banks representing, as it does, largely a bookkeeping transaction with the Federal Reserve Banks, is not important from the standpoint of the money market.

"As an aid in the consideration of problems of open market policy and debt management which this situation requires, estimates of the important elements relating to bank reserves, Treasury balances, and debt retirement by weeks for the first quarter of the year and by months for the half year, based on certain stated assumptions, were prepared by the staff of the Board of Governors, and are given in the attached memorandum.

"On the basis of its consideration of these data the executive committee suggests that the Treasury retire all of the Federal Reserve holdings of certificates and bonds maturing in February, March, and April. In addition, it is suggested that the Treasury retire 100 million dollars of bills each week. On March 18, April 1, and April 8, when maturities are larger than in other weeks, retirements could be increased to 200 million or 300 million if funds are available.

"The question of timing of Treasury withdrawals of funds from the market is complicated by the necessity of support of Government securities prices by the Federal Reserve Banks, which puts funds back into the market. In view of the indicated large withdrawals by the Treasury from bank reserves, it is expected that the banks will sell a considerable amount of Government securities between now and early April in order to maintain their reserves (and thus to maintain their loans and their other investments), and that the Federal Reserve Banks will be the principal if not the only buyers. The amount of securities that the banks will need to sell will be considerably less than the total drain by reason of Treasury transactions, of course, because of the expected inflow of gold and return flow of currency and possible other offsetting factors. The necessary sales by banks will be further reduced to the extent that nonbank holders of Government securities continue to sell part of their holdings and the securities

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"are purchased by the Federal Reserve Banks, an operation which also provides commercial banks with reserve funds. The System's purchases of restricted bonds (sold by non-bank investors) have already exceeded a billion dollars since the beginning of the year. If they continue at this rate, the pressure on banks will be considerably reduced.

"The committee was unanimous in its opinion that pressure on the reserve position of the banks should be exerted continuously throughout this period, in order to restrain further expansion of bank loans, but was divided in its opinion as to whether the means available should practically all be used in the first quarter of the year, or whether some considerable part should be reserved for use in the second quarter. One view was that the maximum possible pressure on the reserve position of the banks should be maintained now; that unless the trend of expansion of bank credit is checked during the first quarter of the year the battle is likely to be lost. The other view was that a steady, persistent pressure would be just as effective as a more concentrated drain on bank reserves now, and that this would permit the retention of some ammunition for use in the second quarter of the year. Those who held the first view advocated much larger withdrawals of Treasury funds from war loan accounts, during the first quarter, than would be desirable if the second view prevailed. Both views took account of the fact that Treasury expenditures will exceed receipts during the second quarter of the year and that Treasury transactions will then be supplying funds to the market. In addition, the banks will no doubt gain reserves, during that period, through continuance of gold inflow. Unless the Federal Reserve System is to be granted additional powers by the Congress, therefore, or unless a substantial Treasury balance is to be left in war loan account (for withdrawal during the second quarter), the means of restraining a further expansion of bank credit will be temporarily exhausted by early April; it being assumed that maintenance of an orderly market in Government securities will continue to be part of our policy, and that substantial sales of Government securities by the Federal Reserve Banks will not be possible.

"In consideration of both views expressed in the committee, and since decision as to the timing of calls on

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"war loan deposit accounts need not be taken immediately, it was agreed that these accounts should be built up to at least a billion dollars and that recommendations as to calls could be made later in the light of developing conditions in the money market.

"No matter which program is followed with respect to calls on war loan accounts, the drain on bank reserves from Treasury transactions and the possible use of powers still available to Federal Reserve authorities, during this period, may result in a further tendency for short-term money rates to rise. This would be especially true if bank loans continue to expand. It is the committee's view that any tendency for short-term rates to rise should not be opposed by System purchases of these securities at existing rates. On the contrary, in these circumstances the committee believes that it would be desirable for the Treasury to refund its March 1, March 15, and April 1 maturities with new issues maturing April 1, 1949, and bearing a coupon rate of 1-1/4 per cent.

"We shall be glad to discuss this program at your convenience."

Later in February, following the decline in commodity prices, Chairman Eccles discussed the above letter with Under Secretary of the Treasury Wiggins who expressed the view that under the then existing conditions the rate on certificates should not be increased to 1-1/4 per cent as recommended in the letter of February 5, but should be deferred perhaps until July. Chairman Eccles understood from the conversation with Mr. Wiggins that a decision on the rate increase in connection with the refunding of March 1 and March 15 maturities would not have to be made until February 20, but on Wednesday, February 11 the Treasury advised that it would be necessary to make a decision the next day. Chairman Eccles discussed

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the matter with Mr. Sproul and it was agreed that an increase in the rate should not be pressed in connection with the March refunding and Mr. Wiggins was advised accordingly on February 13. Subsequently, with the approval of the members of the executive committee (Mr. Szymczak acting in the absence of Mr. Vardaman, and Mr. Gidney acting in the absence of Mr. Davis) the following letter of confirmation was sent to the Secretary of the Treasury under date of February 17, 1948:

"This letter is in confirmation of my recent telephone conversation with Mr. Wiggins in which we discussed the suggestions contained in my letter of February 5, 1948, submitting the views of the executive committee of the Federal Open Market Committee with respect to debt management during the first six months of this year.

"In view of the changes in the situation since our letter was written, including the decline in commodity prices, the members of the executive committee are in agreement with the decision of the Treasury to refund the March 1 and March 15 maturities with a new 1-1/8 per cent certificate issue.

"Another meeting of the Federal Open Market Committee will be held at the end of this month at which further consideration will be given to the desirability of an increase in the certificate rate to 1-1/4 per cent. It may be that at that time the Committee will wish to suggest that the increase be made effective in connection with the refunding of the issue of certificates maturing on April 1, 1948."

Upon motion duly made and seconded, and by unanimous vote, the actions of the members of the executive committee in approving the two letters set forth above were approved, ratified, and confirmed.

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At the meeting of the executive committee on December 9, 1947, the suggestion was approved that further consideration be given at this meeting of the executive committee, and at the meeting of the full Committee which would follow this meeting, to the desirability of a special report to Congress of the kind referred to at the October meeting of the Federal Open Market Committee with respect to the monetary and credit problems with which the Committee had to deal. In a discussion of the matter, Chairman Eccles stated that in view of the developments since the special report had been proposed it was his opinion that it was inadvisable to submit such a report. Mr. Sproul concurred in that view, stating that because of the events that had transpired since last October there would be no point in making the report.

The other members of the committee agreed with the position taken by Messrs. Eccles and Sproul and it was agreed unani-  
mously that a recommendation would be sub-  
mitted to the full Committee that such a  
report be not made.

Preliminary to the discussions at the meeting of the Federal Open Market Committee tomorrow, Mr. Thomas reviewed the estimates that had been made in the Division of Research and Statistics of the Board of Governors of the possible effects on member bank reserves of Treasury receipts and payments during the remainder of the first quarter and during the second quarter of the

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current calendar year. Mr. Sproul stated that there was a very substantial difference, amounting to as much as \$2 billion, in these estimates and the estimates made by the Federal Reserve Bank of New York.

There was a general discussion of the factors which would affect member bank reserves and there was agreement that pressure on reserves undoubtedly would be larger during the remainder of the first quarter than was contemplated when the letter of February 5, 1948, was sent to the Treasury, and that for that reason there should be no withdrawals from war loan accounts during the month of March. It was also the view of the committee that because of the wide variation in the estimates of the net results of Treasury operations during the second quarter it would be difficult to forecast at this time what the situation would be but that the action taken in the period should be directed toward keeping pressure on member bank reserves to the extent that the Federal Open Market Committee had power to do so.

Mr. Sproul raised the question, which was on the agenda for the meeting of the full Committee, whether withheld income tax payments should be channeled through war loan accounts. The opinion was expressed that, while it might not be possible to make the change in procedure in time to have much effect during the current quarter, it would be desirable from the standpoint



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of long-term management of the money market that the change be made, as it would place withheld income tax payments in war loan accounts where they could be held or withdrawn, depending on the effects desired.

Mr. Sproul stated that at the meeting of the Presidents' Conference yesterday he suggested that consideration might be given to refunding the April 1 maturity of certificates with an eleven-month 1-1/8 per cent certificate which would be an indication, but not a commitment, that a higher rate might be established in connection with the June refunding. If that were done, he said, the June 1 and June 15 maturities might be refunded into a 1-1/4 per cent issue. There was a general discussion of the reasons that might be advanced for a further increase in the short-term rate and whether the Treasury would be willing to make such a change. It was agreed that this matter should be considered at the meeting of the full Committee.

At this point Mr. Vardaman withdrew from the meeting to keep another appointment.

Chairman Eccles then referred to the message on housing which the President submitted to the Congress this week and there was a discussion of the adverse effects that the legislation proposed in the message would have on the problem of inflation and credit control. It was agreed that the principal points of the

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legislation should be brought to the attention of the members of the full Committee.

Mr. Rouse stated that, because the Federal Reserve Banks had been the principal buyers of Government securities in the recent period and most transactions in Treasury bonds were at the support prices put into effect on December 24, 1947, some dealers that were not qualified to do business with the System open market account had complained that they had nowhere to turn for the sale of Government securities and that they were being forced out of business. He said that these dealers did a local, as distinguished from a national, business and therefore could not qualify to do business with the System open market account under the terms established by the Federal Open Market Committee in 1944, that the dealers concerned felt that these terms should be given a more liberal interpretation or should be changed to eliminate the alleged discrimination, and that, while the matter had been given very full consideration at the Federal Reserve Bank of New York, it was felt that there was no basis upon which a recommendation could be justified that such action be taken. One of the suggestions that had been made to meet the situation, Mr. Rouse said, was that qualified dealers be permitted to split commissions with the unqualified dealers, and although that proposal had also been given very careful consideration and had been

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studied by Mr. Tiebout, Assistant General Counsel of the Federal Reserve Bank of New York, and Mr. Vest, General Counsel of the Federal Open Market Committee, no satisfactory solution had been found. He added that Mr. Tiebout had submitted an opinion to the effect that such an arrangement would raise the question of the application of the Clayton Antitrust Act and, in order to provide the necessary controls, it would be necessary to make the unqualified dealers subagents of the Federal Reserve Banks which would involve entering into an arrangement which the New York Bank would not recommend. Mr. Rouse made the further statement that he was much less concerned about the problem now than when it was first raised for the reason that, on the basis of informal reports made to him by two of the unqualified dealers, the situation is righting itself and they were not suffering serious losses of earnings.

He said that an application from the Northern Trust Company of Chicago to qualify as a dealer had been denied on the basis that its business was confined largely to the Chicago area and was not national in scope, that an application had been received also from the Chemical Bank and Trust Company of New York, and that on the basis of preliminary information it appeared that that bank would be able to qualify.

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Chairman Eccles suggested that the Federal Reserve Bank of New York submit to the executive committee a memorandum of the consideration which it had given to the problem presented by the unqualified dealers, together with a recommendation as to what, if any, action might be taken. Such a recommendation, he said, could be discussed at the next meeting of the executive committee and a recommendation made to the full Committee so that in the event of further complaint it could be shown that the position of the Committee had been taken only after complete consideration of all of the questions involved.

Upon motion duly made and  
seconded and by unanimous vote,  
this suggestion was approved.

Mr. Rouse then stated that sometime ago it had been ascertained that there had been periods when the reserve position of dealer banks in New York was affecting their ability to act as Government security dealers, but that in all other respects they had been discharging their dealer functions as effectively and in some respects more effectively than the nonbank dealers. To meet that situation, he said, he had asked for written assurance from each of the New York dealer banks that a stated amount of funds would be available at all times for use in the bank's business as a dealer. He added that such assurances had been given and that it was proposed to get the same assurances from

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dealer banks in Chicago as soon as convenient.

Thereupon the meeting adjourned.

Chester Morris  
Secretary.

Approved:

W. H. ...  
Chairman.