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, October 11, 1950, at 2:30 p.m.

PRESENT: Mr. McCabe, Chairman
Mr. Sproul, Vice Chairman
Mr. Eccles
Mr. Evans
Mr. C. S. Young

Messrs. Erickson, Peyton, Powell, and Vardaman, Members of the Federal Open Market Committee

Mr. Morrill, Secretary
Mr. Carpenter, Assistant Secretary
Mr. Vest, General Counsel
Mr. Thomas, Economist
Messrs. Langum, Neal, and Williams, Associate Economists
Mr. Thurston, Assistant to the Board of Governors
Mr. Riefler, Assistant to the Chairman, Board of Governors
Mr. Sherman, Assistant Secretary, Board of Governors
Mr. Wurts, Assistant Vice President, Federal Reserve Bank of New York
Mr. Ralph A. Young, Director, Division of Research and Statistics, Board of Governors
Mr. Youngdahl, Chief, Government Finance Section, Division of Research and Statistics, Board of Governors
Mr. Leach, Economist, Division of Research and Statistics, Board of Governors

There was a discussion of the action to be taken by the executive committee in order to carry out the instructions issued by the Federal Open Market Committee at its meeting this morning. During the discussion, Mr. Sproul suggested that the issuance of the usual general direction to the New York Bank for the execution of transactions for the System account and the adoption of substantially the motion made and lost on a tie vote at the meeting of the executive committee on October 5 would provide the necessary instruction to the New York Bank for this purpose.

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 current and prospective economic conditions and the general credit situation of the country, with a view to exercising restraint upon inflationary developments, to maintaining orderly conditions in the Government security market, to relating the supply of funds in the market to the needs of commerce and business, and to the practical administration of the account; provided that the total amount of securities in the account at the close of this date shall not be increased or decreased by more than $2 billion 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 million.

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

Mr. Sproul then moved that, pursuant to the action taken at the meeting of the Federal Open Market Committee on September 28, 1950, as reaffirmed at its meeting today, the Federal Reserve Bank of New York be instructed to take such action, in accordance with the direction issued by the executive committee today, as may be necessary (a) to allow the market yields for Treasury securities on a one-year basis to move up to the highest point, not exceeding 1 1/2 per cent, which will not result in such pressure on the longest term restricted bonds as would cause continuing purchases in substantial amounts of long-term bonds for the System account, (b) to prevent market prices of the longest term restricted bonds from declining in response to market conditions to below a point between 4/32 and 8/32 above par, and (c) to maintain an orderly market while carrying out the above instructions.

Mr. Sproul's motion was put by the Chair and carried unanimously.

In a discussion of the ranges at which short-term Treasury securities might be purchased and sold by the Federal Reserve Bank of New York in carrying out the foregoing instruction, Mr. Sproul suggested that a range of 1.30-1.49 per cent on a one-year basis on securities maturing or callable within one year would be satisfactory. Mr. Eccles suggested that the New York Bank be authorized, within the limitation of 1.49 per cent, to vary the rate at which it will purchase and sell Treasury bills as, in its judgment, may be required in the light of current conditions in the money market to carry out the general policy of the Federal Open Market Committee.

These suggestions were approved unanimously.

It was also agreed that there should be no change at this time in the understanding that replacement of System maturing bill holdings should be guided by what would be required in the light of current conditions in the money market to carry out the general credit policy of the Federal Open Market Committee.

There followed a discussion of the procedure that the New York Bank might adopt in carrying out the committee's instruction with respect to purchases of long-term bonds. Mr. Sproul stated that the main purpose of System policy was to avoid putting funds into the market and that purchases of bonds should seek to support this objective. He also said that the timing and volume of bond purchases would depend on market conditions and if fewer funds would be put into the market by holding at about present levels while short rates were advancing or by permitting a gradual decline in prices of the long-terms, that course should be followed, but that if, while short rates were increasing or they were increased or for any other reason, offerings of bonds were heavy, it would be desirable to let prices decline rapidly.

> It was agreed unanimously that the procedure suggested by Mr. Sproul with respect to long-term bonds should be followed by the New York Bank.

In connection with a discussion of how soon short-term rates could be expected to increase to 1 1/2 per cent on a one-year basis, Mr. Sproul suggested that in order to avoid confusion in the bidding for Treasury bills next Monday, action by the New York Bank in beginning to carry out the instructions of the executive committee with respect to the short-term rate be deferred until Tuesday of next week. Thereafter, he said, the New York Bank would attempt to proceed gradually with the increase in the one year rate, but the market might force more rapid action.

This suggestion was approved unanimously.

In accordance with the action of the full Committee, it was understood that the staff would prepare a draft of a statement of the reasons for the current policy of the Federal Open Market Committee which would be in a form suitable for the policy record.

Chairman McCabe suggested that the committee authorize the preparation of a letter with respect to current System credit policies, which, after approval by the Board of Governors and the members of the executive committee, would be sent by him as Chairman of the full Committee and the Board to the Secretary of the Treasury.

Chairman McCabe's suggested general procedure was approved unanimously.

Secretary's Note: The following letter, having been approved by the Board of Governors at a meeting on October 13, 1950, and over the telephone by Messrs. Sproul and Young on October 13, 1950, respectively, was sent to Secretary of the Treasury Snyder on October 16:

"Two weeks ago Mr. Sproul and I discussed with you the problems of the Treasury and the Federal Reserve System in the fields of debt management and credit policy, as parts of the broader anti-inflationary policy and program of the Government. At that time, the Federal Open Market Committee was in session and we conveyed to you its thinking on open market operations, as well as the thinking of the Board of Governors on reserve requirements and selective controls. Your views, which you then expressed to us, were in turn conveyed to the Federal Open Market Committee, as was your suggestion that you would like a couple more days to think over the matters we had talked about.

"The Federal Open Market Committee, in response to our report of our conference with you, asked its Executive Committee to carry forward these discussions, and it was in response to this direction that Mr. Sproul and I again sought a conference with you before a meeting of the Executive Committee of the Federal Open Market Committee on October 5. In that conference, we told you of the unanimous view of the Federal Open Market Committee, and of the Board of Governors, that further action should be taken in the field of general credit control to put a brake upon the prevailing ease with which banks can obtain reserve funds for further credit expansion. You told us of your concern about the success of the forthcoming Savings Bond Campaign and of the discussions which have been started to put in motion voluntary action by the commercial banks to restrain credit expansion. At that meeting you also said that you would like to have an opportunity to talk with me again on the following Monday.

"You and I have since talked two or three times on the telephone and, in the light of these conversations and of our earlier conferences, a meeting of the Federal Open Market Committee was called for Wednesday, October 11. At that meeting your views, as they had developed in our talks, were given fully and frankly to the Committee. As you know, the Committee also expressed its willingness to have you present these views in person if you so desired. You decided, and I think properly, not to deviate from the established procedure which we have adopted for mutual consultation.

"After giving thoughtful consideration to your views, the Committee again canvassed the business and credit situation as developed by the reports and studies of its research staff and through the contacts of members of the Committee in various parts of the country. It seemed clear to the Committee that, despite some signs or prospects of moderate abatement of inflationary pressures which might be detected in certain fields, the underlying forces in our economy are still strongly inflationary and will be accelerated by increasing Government expenditures as the rearmament program really begins to bring its huge demands upon our economy, unless stern fiscal policies such as you have advocated and further credit restraints are adopted.

"The President announced the anti-inflationary policy of the Government when, in the Midyear Economic Report, he stated that:

'First of all, for the immediate situation, we should rely in major degree upon fiscal and credit measures.

"'These general measures can be helpful not only in restraining inflationary pressures, but also in reducing the civilian demand for some specific products, such as automobiles and housing, thus making available for necessary military use a larger proportion of an already short supply of some critical materials. The more prompt and vigorous we are with these general measures, the less need there will be for all of the comprehensive direct controls which involve the consideration of thousands of individual situations and thus involve infinitely greater administrative difficulties and much greater interference with individual choice and initiative.'

In the light of this policy and of the statutory responsibility of the Federal Open Market Committee, which provides that the time, character, and volume of open market operations shall be governed with a view to accommodating commerce and business and with regard to their bearing upon the general credit situation of the country, the Committee felt that it had no option but to proceed with the action we had advised you orally, two weeks ago, that it had in mind. Since the Treasury will have no refunding operations until December, the present is an especially propitious time for the System to proceed with this somewhat more restrictive open market policy, even though the action results in a moderate increase in short-term rates. Any resultant increase in the costs of carrying the public debt will be directly saved, many times over, if it helps to curb the rising costs of Government procurement, and the benefits to the people of the country, of course, will be greatly multiplied.

"We realize that the action we are taking in our open market operations will need to be supplemented in order to exercise effective restraint on the mounting inflationary pressures that threaten the economy. Consequently, we are unanimous in the conviction that we can only meet our responsibilities by going ahead with the weapons at our command, including increases in reserve requirements, application of real estate credit controls, and tightening up of consumer credit regulations. We sincerely believe that the combination of these restraints on credit expansion will have a profound effect in the effort to hold the line until the heavier taxation promised for next year begins to bite into incomes.

"We can assure you that these actions will not affect the maintenance of the 2 1/2 per cent rate for the outstanding longest term Government bonds, and we are convinced that this further evidence of a resolute will to fight inflation and to protect the purchasing power of the dollar will promote, not discourage, the sale of E bonds. No one knows better than you that confidence in

"E bonds, as well as all other types of savings, is based on confidence in the purchasing power of the dollar.

"Although in this instance we have not been able to bring about a complete meeting of minds in our discussions with respect to System policy and debt management, we have both thoroughly considered all of the aspects of the difficult problems confronting us and we have earnestly sought to achieve that accord which I know you desire as much as we do in meeting our respective responsibilities. At your convenience we would like to sit down with you to explore further the problems for which we both seek solutions that are in the best interests of this country."

Thereupon the meeting adjourned.

Chester Morrill
Secretary.

Approved:

Thomas B. McCabe
Chairman.