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, August 8, 1951, at 2:35 p.m.

PRESENT: Mr. Martin, Chairman
Mr. Sproul, Vice Chairman
Mr. Szymczak
Mr. Williams
Mr. Evans (alternate member)

Mr. Carpenter, 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. 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
Mr. Arthur Willis, Special Assistant, Securities Department, Federal Reserve Bank of New York.

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the executive committee held on June 27, 1951, were approved.

Mr. Rouse presented and commented on a report prepared at the Federal Reserve Bank of New York covering open market operations for the System open market account during the period June 27 to August 6, 1951, inclusive. He also presented a supplementary report covering commitments executed on August 7, 1951. Copies of both reports have been placed in the files of the Federal Open Market Committee.

In connection with his report, Mr. Rouse stated that the Federal Reserve Bank of New York had entered into repurchase agreements covering Treasury bills much more frequently during the recent period than was contemplated when the authority was originally given, that such broader use was indicated during the discussion at the meeting of the Federal Open Market Committee on March 8, 1951, and that the agreements had demonstrated their usefulness as an effective instrument and should continue to be available.

Mr. Rouse also stated that the Federal Reserve Bank of New York had reviewed the basis for the allocation of securities in the System account in the light of the earnings and expenses of the Federal Reserve Banks for the first six months of 1951 and that it was not felt that any change in the basis was called for at this time.

> Upon motion duly made and seconded, and by unanimous vote, the transactions in the System open market account as reported to the members of the committee for the period June 27 to August 7, 1951, inclusive, were approved, ratified, and confirmed.

Chairman Martin suggested that it would be helpful if Mr. Rouse's report on open market transactions could be placed in the hands of the members of the executive committee in advance of the meetings. Mr. Rouse said that he would follow the same procedure as was being used in connection with similar reports for the meetings of the full Committee which contemplated that the report would be made available to the members of the committee at least a day before the meeting of the committee.

Chairman Martin reported that he had been informed by the Treasury that a decision had been reached not to call the issue of 2 per cent, December 15, 1951-55, bonds in the amount of $510 million, but that the issue of 2-1/4 per cent, December 15, 1951-53, bonds in the amount of $1,118 million would be called. It was understood, he said, that announcement of this decision would be made on Monday, August 13.

Before this meeting there had been sent to the members of the committee copies of memoranda prepared by the staff under dates of August 6 and 7, 1951, respectively, with respect to (1) the outlook for bank reserves and Treasury cash requirements and (2) alternative programs for refunding the Treasury issues of bonds and notes maturing from September 15, to November 1, 1951, inclusive.

Chairman Martin stated that it would be desirable at this meeting to have a preliminary discussion of the recommendations to be made to the Treasury with respect to refunding and to have another meeting of the executive committee during the latter part of August at which time final decisions would be reached on the recommendations to be made to the Treasury. This procedure was agreeable to the other members of the committee and it was understood that another meeting of the committee would be held during the week of August 20 or, in any event, not later than August 27.

As a preliminary to a discussion of Treasury financing and

instructions to be issued to the Federal Reserve Bank of New York with respect to transactions for the System open market account, Mr. Thomas stated that at the moment the economic situation was pretty well balanced; there seemed to be a possibility that further inflation might be avoided, but little or no likelihood of a serious downward movement in prices, consumption, production, or employment. A resumption of strong inflationary pressures was decidedly not out of the picture. He stated that the principal unknown factor in the situation was the volume of defense expenditures; if these expenditures increased according to schedule then a renewal of inflation was probable. The volume of capital expenditures is expected to continue very large and consumer buying may again increase. On the other hand, the inventory expansion will most likely come to an end, releasing more of current output for current use, and a substantial decline in housing construction is now taking place. While the situation might continue fairly well balanced during the remainder of the year, he did not believe that would be the case if restrictive measures were relaxed to any great extent.

He then discussed the outlook for bank reserves and Treasury cash requirements, as outlined in the memorandum above referred to, and the possible effects of debt management and Federal Reserve credit policies. On the basis of the prospective Treasury deficit and of a projected loan expansion of about half that of the last half of 1950, the money supply might show a further expansion of as much as $7 billion during the

remainder of the current year. Such an expansion would be as great as that of the same period last year and would be an inflationary influence. It might be kept down by continued Federal Reserve policies of credit restraint and Treasury offerings of new securities attractive to nonbank investors.

During Mr. Thomas' statement, Mr. Riefler, Assistant to the Chairman, Board of Governors, joined the meeting.

Mr. Young commented that the outlook for continued large supplies of consumer goods, as well as basic materials such as farm crops were factors which would work against further inflation but that, if the increase in the money supply was as large as outlined by Mr. Thomas, very sharp inflationary pressures could be expected to reappear. The result, he said, was a very mixed outlook with a number of uncertainties to be resolved. He added that a spot survey in leading centers had indicated very little response on the part of consumers to the relaxed terms under Regulation W, Consumer Credit. He also said that the number of housing starts in July was not yet available, but that representatives of the Housing and Home Finance Agency were of the opinion that the direction of housing activity was decidedly downward toward a level by the end of the year which would be below the goal regarded as desirable. The information assembled by the staff of the Board of Governors, however, did not indicate as pessimistic a picture as that,

Chairman Martin observed that it would not be possible to make a forecast as to the future in the absence of information as to what the level of defense expenditures would be. In that situation, he said, it would be necessary to "play by ear" until more definite information was available and in the event the expected volume of defense production did not materialize it would be necessary to be prepared to meet the appearance of deflationary developments.

In a discussion of the problem before the committee in the light of possible developments, Mr. Sproul made a statement substantially as follows:

> The lull in the inflationary situation has continued longer than at first contemplated and it might go further. Any substantial movement from the present level is much more likely to be inflationary than deflationary. Much depends on the rate of increase in defense expenditures and on the unpredictable factor of what the public will do with a very high level of current income and very large holdings of liquid assets. In terms of credit policy, the situation suggests the maintenance of the status quo and of the present degree of restraint on credit expansion (which is not very great and will not be greater during the period of Treasury refunding) and continued alertness to the possibility of having to tighten restraints if inflationary pressures reassert themselves.
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> On the question of debt management, while the estimates now show a deficit for the fiscal year 1952, it is quite possible and probably more realistic to think in terms of expenditures being somewhat less than estimated and income being somewhat more, so that if a tax bill is enacted to take effect during a part of the fiscal year it will be possible that the cash budget may be balanced or show a modest surplus. That would mean Treasury borrowing during the first half of the year which would be paid off during the second half. Therefore, we should consider the problem of borrowing and refunding together. There are many possible combinations that could be used in approaching the problem. I start on the basis that borrowing should continue to be aimed at

trying to get as much nonbank money as possible and to fill in the quarterly maturity dates. As I see it now, I would discard the suggestion of doing the September-November refunding in one operation as that would run the risk of greater attrition than would be the case with a divided operation. It also involves the risk of a larger amount of bank financing and of bringing the Treasury into the market before it actually needs the funds. I have some bias against an intermediate note, particularly because some bank borrowing will be necessary and we are going to have to supply reserves to the market. In that situation the financing should be done through the medium of short-term, low-rate issues. I would not want to have it implied that we should commit ourselves to the support of any intermediate rate during the next month or two.

Among the various alternatives of refunding, the preferable method would be a simple refunding of the September 15 and October 1 maturities with a 1-7/8 per cent, 9-1/2 month, certificate maturing on July 1, 1952. Then the October and November note maturities could be refunded with a 11-1/2 month, 1-7/8 per cent certificate maturing on October 1. The Treasury could continue to offer $200 million of additional bills each week or $100 million a week and possibly a 6 months tax anticipation note which would be paid off in March when tax payments come in. The December refunding and final new money needs could be handled by issuing a 12-1/2 months note at a rate to be determined at the time in the light of developments and on the basis of whether the situation called for the easing or tightening of restraints.

Chairman Martin inquired whether any member of the committee felt it would be advantageous to do the September-November refunding in a single operation and the ensuing discussion indicated agreement with Mr. Sproul's approach and with the comment made by Chairman Martin that a decision on the refunding of the September 15 and October 1 bond and note maturities only should be made toward the latter part of this month.

Reference was again made to the question whether the Treasury should continue through the present cycle of bill offerings to raise $200 million of new money each week or whether additional funds should be raised

in some other way.

Mr. Rouse stated that the committee was faced with the immediate problem of whether the market rates on Treasury bills should be allowed to continue to rise, which could affect the rate at which the forthcoming refunding would be done. As he saw it, it was a question whether the System would supply reserves to the market more freely and thereby limit the increase in rates or whether the market should be permitted to determine the rate with the understanding that Treasury refunding would be determined in the light of what market influences had done to the rate structure.

Chairman Martin stated that the committee should consider that question and whether it would be desirable to discontinue for a few weeks the raising of further funds through increased bill issues. In that connection, Mr. Rouse referred to the increase in the rates on bills during the last two weeks and the fact that prior to that time the increase in the weekly issues had been taken largely by nonbank sources whereas during the last two weeks there had been a slackening in the nonbank demand and a supply of offerings from the substantial purchases by banks. He also said that the decision had already been made by the Treasury to continue the increased bill offering next week, that the money market probably would be somewhat easier during the following week, and that, therefore, the increased offerings might be suspended beginning with the succeeding week.

In the ensuing discussion it was the consensus that, on the basis of the present policy of neutrality, the bill rate should not be permitted to increase to a point where it would affect adversely the 1-7/8 per cent rate on the two outstanding issues of Treasury certificates.

Chairman Martin referred to the understanding at the meeting of the committee on June 27 that the Federal Reserve Bank of New York would not permit the price on the longest-term restricted Treasury bonds to decline below 96-3/4 and he raised for discussion the question whether there should be any change in that understanding.

Mr. Rouse stated that there were indications about two weeks ago that the prices of longer-term bonds might decline further and that at that time the committee might be faced with the problem whether the market on the longest-term restricted issues should be permitted to go below 96-3/4. However, he said, the market had since moved up to a point where at least for the time being the question was an academic one. It was his view that if the question should arise again before another meeting of the committee it would be preferable to allow the decline to go to a point slightly lower than 96-3/4 without interference by the System except for the purpose of maintaining orderly market conditions.

In a discussion of this point, during which Mr. Sproul suggested the possibility of intervening at some point above 96-3/4 in an effort to

determine whether it would be possible by limited purchases to keep the market from going back to the 96-3/4 level, it was agreed that no change should be made in the understanding as stated in the meeting on June 27, 1951.

It was the opinion of the members of the committee that no change should be made in the existing direction to the Federal Reserve Bank of New York to execute transactions for the System account.

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:

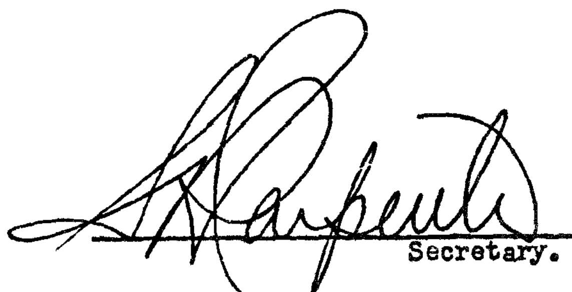
(1) To make such purchases, sales, or exchanges (including replacement of maturing securities and allowing maturities to run off without replacement) for the System account, either in the open market or directly from, to, or with the Treasury, as may be necessary in the light of current and prospective 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 $1 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

would include commitments for purchases and sales of securities for the System account.

Thereupon the meeting adjourned.



Secretary.