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 Monday, September 15, 1952, at 10:30 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Sproul, Vice Chairman
Mr. Hugh Leach
Mr. Mills, Alternate
Mr. Vardaman

Messrs. Evans, Robertson, and Szymczak, Members of the Federal Open Market Committee

Mr. Riefler, Secretary
Mr. Vest, General Counsel
Mr. Thomas, Economist
Mr. Young, Associate Economist
Mr. Rouse, Manager, System Open Market Account
Mr. Sherman, Assistant Secretary, Board of Governors
Mr. Ralph Leach, Acting Chief, Government Finance Section, Division of Research and Statistics, Board of Governors
Mr. Willis, Assistant Secretary, Federal Reserve Bank of New York

Before this meeting there had been distributed copies of a report prepared at the Federal Reserve Bank of New York covering open market operations during the period August 29 to September 10, 1952, inclusive, as well as a supplementary report covering commitments executed on September 11 and 12, 1952. Copies of both reports have been placed in the files of the Federal Open Market Committee.

Upon motion duly made and seconded, and by unanimous vote, the transactions in the System open market account for the period August 29 to September 12, 1952, inclusive, were approved, ratified, and confirmed.

Chairman Martin referred to a memorandum prepared by Messrs. Riefler, Thomas, and Ralph Leach under date of September 11, 1952, on credit developments and Federal Reserve policies, copies of which had been sent to each member of the committee before this meeting. Following a brief comment by Mr. Thomas on the economic and credit situation, Chairman Martin made a statement substantially as follows:

> "I want to report on the discussions I had with the Secretary of the Treasury while I was in Mexico City. I started out with the Secretary on Labor Day, September 1, at which time I told him about the meeting of the executive committee that had been held on August 29, 1952. I told him that open market policy seemed to be clearly set forth in the letter we had sent to him on July 23, 1952, and that I thought it very important that the Treasury issue to be put out in connection with the October 1 refinancing be priced in accord with the market. I told him at that time that I thought a rate of 2-1/8 per cent was going to be required. He was not extremely receptive to going to that rate. He had been very hopeful of doing the job on a 2 per cent basis, and he had been encouraged to believe it could be done on that basis but when the certificate rate got above 1.94 or 1.95 he agreed it was going to be difficult. I urged him strongly to do the whole thing on a straight roll-over basis. I made it very clear this was my individual opinion and not an Open Market Committee action. (I have come to question more and more this business of indicating a rate to the Secretary and writing a letter and getting into something of a contractual relationship.) I said that if he was going to come out with something lower than a 2-1/8 per cent rate, I thought it would be desirable to delay the announcement until the executive committee had had a chance to review the financing, and that I personally thought he could not do it for less than 2-1/8 per cent. I think an announcement could have been held off until this afternoon but it did not seem important to do so and the Treasury people were anxious to get it out ahead of the new issue of housing bonds.

"While we were in Mexico City I spent a great deal of time with the Secretary in discussions of this refinancing. In our discussions, he said that he would like to have my opinion on a 14-month note and I said that I would give him my personal clearance, that I would come back to the committee and discuss the proposal, and that I knew the committee would give every support that it could to make the issue a success. I said that I did not wish to be in the position of giving him the impression of speaking for the committee when the committee was not in session, but that I felt very clear that the policy set out in our letter of July 23 was the policy within which he should operate. As you know, the announcement of the 2-1/8 per cent 14-month note was issued after the close of the market last Friday and in talking with the Secretary this morning I assured him that the purpose of this meeting was to discuss the most effective means of making the issue acceptable. I pointed out to him that we did not want attrition on the Treasury offering any more than he did, but that we had a credit and monetary policy to pursue.

"I think that this morning we should consider the best course for us to pursue during the 4 days that the books on this new financing are open. I would suggest that we take up the memorandum that has been prepared by the staff which seems to me to offer a very good basis for discussion."

Mr. Sproul then made a statement substantially as follows:

"There are various ways in which we might operate in the market during this period. My estimate of the situation from having followed the market very closely during the past few weeks is that the offering of the 2-1/8 per cent security of December 1, 1953 will please no one very well. The substantial number of nonbank holders of maturing certificates are still believed to prefer something with one year or less to run. The market as a whole will consider that this means an upward adjustment in the one year rate, not paying too much attention to the added two months, so that those who argued for no change in rates at this time will not be comforted. There may, therefore, be a downward adjustment in prices all along the line. On the other hand, sellers of 'rights' may buy shorter issues and give support to this area of the market including bills.

"Our general policy as formulated at the last meeting of the committee was to continue the controlled release of reserves through open market operations, while keeping the banks under pressure to borrow. Various guides to execution of policy were discussed at that meeting although none was formally adopted. Since that meeting, $24 million of bills have been purchased for the System account to help relieve pressure over the Labor Day weekend and other factors have greatly improved the reserve position of banks. The money market still remains tight, however, in terms of available funds, rates to dealers, and other factors. Following the announcement last Friday, it is understood that the Treasury is going to let its balances run down perhaps $300 million and this, plus an increase in float estimated around $300 million, should provide a substantial amount of funds to the market despite an increase in required reserves.

"It was understood at the last meeting of the executive committee that support operations for the October 1 Treasury financing should be of the same character as in the case of the August 15 refunding, and that there should be no innovations. The market would be left to determine what the premium, if any, should be on the new issue. This means that beginning this morning, we shall buy 'rights' freely at par, and will buy other issues of one year or less if their prices should decline to a point which would threaten the par bid on the 'rights'. (Temporarily, at least, such support of other issues may be unnecessary.) There would be no selling or swapping to offset purchases unless and until the volume of our outright purchases becomes so great as to endanger our credit policy.

"Now as to the positions taken in the memorandum from Messrs. Riefler, Thomas, and Leach: the whole range of positions is tied together. I would like to give you my views and to hear the views of others, but before doing this let me say that I agree with the position Chairman Martin took, personally, that the System should give whatever support to this 2-1/8 per cent issue it can, but such support should be within the limitations of our credit policy.

"On the points set out on the third page of the staff memorandum, number 1 suggests an offering of a 2-1/8 per cent "security with a maturity of not more than 14 months. That has now been announced by the Treasury. Number 2 suggests that during the period after the announcement and until the close of the books the System should be prepared to purchase Treasury bills at a rate of about 1.85 per cent--approximately the high of dealers' bid rates prevailing in recent weeks. On this point of protecting the new issue, I think the market which is most likely to take care of itself without our intervention is the bill market. If, to protect the new issue, however, we are forced to 'interfere with market forces and the appropriate price relationships', a peg of 1.85 for bills seems to me to be too low. That would be a peg based on a bill rate established in a 2 per cent market for one year. I don't think we can or should try to hold the rest of the market down with such a rate on bills. On the third point of paying a premium of 1/32 on the maturing issue: that is probably not enough to give strong support to the new issue but is still enough to transfer attrition from the Treasury to us and thus to weaken our control of reserves. I would rather have the attrition go to the Treasury. On number 4 regarding the avoidance of swaps, when widely diverse owners of $4 billion of securities have to decide in three or four days whether to exchange, or swap, or cash-in, and when market psychology is so important, we can't rely on perfect arbitrage in the market and the immediate development of appropriate price relationships. In order to avoid too great increase in our portfolio, some swapping may become desirable. As to number 5, that System purchases of outstanding issues maturing around the same time as the new issue should be avoided, the choice may be between giving some support to outstanding issues maturing at about the same time, or buying the maturing issue from frightened sellers, which we then will have to exchange for the new issue. In the latter case, the System's portfolio may become more heavily loaded with issues not easily disposed of than in the former case. On number 6, I see no need to consider purchases of the new issue on a when-issued basis after the books on the offering have been closed and agree that such purchases should be avoided.

"As a general comment on the suggestions contained in the staff memorandum, the committee can do whatever it wants, of course, but I think it is a serious mistake for it to try to give too detailed instructions to the man who executes policy "in a market situation which changes from day to day and hour to hour."

Chairman Martin responded to Mr. Sproul's last statement by commenting that he felt there was a twilight zone within which there needed to be a distinction between instructions relating to policy and those relating to operations. He recalled that a change from earlier procedures was made in connection with the August 15 Treasury refinancing and that there had been a difference in judgments as to how successful the offering had been in view of the relatively large attrition that went to the Treasury. He felt that this was a matter on which the committee should exercise judgment, stating that if the committee felt there would be less attrition in the new financing by following certain procedures, it would be desirable for it to indicate those procedures for carrying out operations in the System open market account.

Mr. Sproul stated that he agreed with Chairman Martin on this point, that he felt this was the type of problem on which the committee should make a judgment.

Chairman Martin then suggested a discussion of the specific suggestions set out in the staff memorandum, adding that his general feeling was that the October 1 financing was of sufficient importance to warrant the committee's doing everything possible to make the issue a success, and that it would be better for the System to take a little attrition on itself and to dispose of securities later on than to open itself to any criticism that it had not done all that it could to make the issue a success.

There followed a long discussion of the proposals contained in the staff memorandum during which Mr. Sproul took the position indicated earlier in his statement, namely, that it was undesirable for the System to "peg" a rate on Treasury bills, and that in any event a rate of 1.85 per cent as suggested was too low; that purchases of the maturing issues if made above par should be at a sufficient premium to give strong evidence of the intent of the System to support the issue which would call for more than a premium of 1/32, and that it would be an unnecessary interference with possibly desirable operations to indicate in advance that swaps of other issues for maturing issues should be avoided since in his opinion some swapping might become desirable. Mr. Sproul added, however, that he agreed that the Open Market Committee should give support wholeheartedly to the Treasury offering so as to make it a success within the limits of the credit and monetary policy adopted by the Committee.

During the discussion, Chairman Martin stated that the problem was one of market judgment and of working with different views as to what constitutes the market, that he would have preferred a 2-1/8 per cent, 12-month issue and had so indicated to the Secretary of the Treasury, but that in his judgment the offering made by the Treasury was a good one that was priced very close to if not on the market, and that he was impressed with the suggestions contained in the staff memorandum as a means of minimizing, within the credit policy of the Committee, attrition on this issue. While the market was learning more and more what to expect in connection with System operations, the Committee had been accused, unjustly at times, of not giving sufficient consideration to the Treasury's problems, and it was his conviction that the committee should not do anything that would add to the amount of attrition the Treasury would have to take in the current financing. The 2-1/8 per cent 14-month issue was close enough to the market to raise a reasonable doubt as to how it would be received and, as he had indicated at the meeting on August 29, the Chairman felt the Committee should "lean over backwards" to show good faith until it had completely determined just what its underwriting responsibility was. This, he said, was the real heart of the problem: that is, whether the Committee would in the end say that it had no responsibility as an underwriter of Treasury offerings other than in connection with determination of monetary and credit policy. He felt it was a little early for the Open Market Committee to take a position that it had no responsibility other than for credit and monetary policy; if such a position were to be taken, the entire

Federal Open Market Committee, rather than the executive committee, should take the responsibility.

At the conclusion of the discussion, during which various suggestions and counter-suggestions were made concerning the proposals contained in the staff memorandum, the committee agreed, by unanimous vote, that the following procedures would be observed in connection with the October 1 Treasury financing announced on September 12, 1952:

(1) During the period until the close of the books, the System without fixing a ceiling of 1.85 per cent should be prepared to purchase Treasury bills at a rate of about 1.85 per cent--approximately the high of dealers' bid rates prevailing in recent weeks.

(2) The System should also be prepared during the same period to purchase any of the maturing issue at a premium of 3/64 to dealers as principals.

(3) It would be understood that during the period until the close of the books the management of the open market account would take into consideration the discussion of the executive committee concerning operations involving swaps of other issues from the System account for the maturing issue.

(4) Purchases of the new issue on a when-issued basis after the close of the books should be avoided.

In response to a question from Chairman Martin, Mr. Rouse suggested that no change be made in the limitations in the general direction to be issued by the executive committee to the Federal Reserve Bank of New York.

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 (including purchases made in connection with week-end transactions under the special authorization of the Federal Open Market Committee dated June 19, 1952) shall not exceed $1 billion.

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.

Chairman Martin stated that the next meeting of the executive committee would be held on Thursday, September 25, the day on which a meeting of the full Committee also would be held.

Thereupon, the meeting adjourned.

Winfield W. Riefler
Secretary