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 on Tuesday, June 23, 1953 at 10:30 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Sproul, Vice Chairman
Mr. Erickson
Mr. Mills
Mr. Szymczak, Alternate for Mr. Evans

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

Mr. Riefler, Secretary
Mr. Thurston, Assistant Secretary
Mr. Vest, General Counsel
Mr. Thomas, Economist
Mr. Carpenter, Secretary, Board of Governors
Mr. Sherman, Assistant Secretary, Board of Governors
Mr. Youngdahl, Assistant Director, Division of Research and Statistics, Board of Governors
Mr. Arthur Willis, Assistant Secretary, Federal Reserve Bank of New York
Mr. R. F. Leach, Chief, Government Finance Section, Division of Research and Statistics, Board of Governors

Upon motion duly made and seconded, and by unanimous vote, the action of the members of the executive committee in increasing, effective June 16, 1953, from $1 billion to $1.5 billion the limitation contained in the second paragraph of the directive issued to the Federal Reserve Bank of New York on June 11, 1953 authorizing the purchase direct from the Treasury of special short-term certificates of indebtedness, was approved and ratified.

Before this meeting there had been sent to the members of the committee a report prepared at the Federal Reserve Bank of New York covering operations in the System open market account from June 11 to June 19, 1953, inclusive. At this meeting Mr. Sproul presented a supplementary report covering commitments on June 22, 1953 and commented on both reports, copies of which 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 June 11 to June 22, 1953, inclusive, were approved, ratified, and confirmed.

Mr. Thomas reviewed economic and financial conditions and prospects along the lines covered in a memorandum prepared by the staff under date of June 19, 1953, copies of which were distributed before this meeting. In his remarks Mr. Thomas stated that the economy continued very strong with some elements of weakness indicated but not very evident. Production was continuing at a very high level and while there has been some accumulation of inventories, generally speaking they do not appear large in relation to current distribution. During his comments, Mr. Thomas referred to a poll of economists soon to be published which showed wide agreement on a forecast that there would be a decline in economic activity this year extending into 1954 and 1955. He reported that at a meeting of business economists held last week strong views to the contrary were expressed by a number of the participants, although most felt that there would be adjustments in economic activity of varying degrees during the next year or two. The general impression, Mr. Thomas noted, was that monetary and credit policy during the coming months would not be tight.

Chairman Martin then called on Mr. Leach, who summarized prospects for Treasury financing requirements. In his comments Mr. Leach indicated that new cash financing needs of the Treasury during the rest of this year would range around $11 to $13 billion with allowance for attrition on maturing issues. Mr. Leach felt that it would be desirable for the Treasury to make an offering of somewhere around $6 billion promptly which would take care of its needs until mid-September when tax anticipation bills might be issued. In his opinion, the best means of obtaining the funds would be to sell four additional issues of Treasury bills at the rate of $1-1/2 billion a week at the end of which time Treasury bills would be on a 17-week cycle, each issue maturing in 119 days. This would avoid having a single large offering face the market at any given time, it would "clear the decks" and remove uncertainty as to the Treasury's total borrowing needs in the immediate future, and it would remove the necessity for the Treasury to price an issue during a period when it was virtually impossible to know what the rate on a certificate or note sold on an interest bearing basis should be.

Chairman Martin noted that the substance of the plan suggested by Mr. Leach had been sent to Mr. Sproul. He also referred to discussions he had had with Mr. Burgess, Deputy to the Secretary of the Treasury, adding that he was under the impression that the American Bankers Association Committee on Government Borrowing would prefer a certificate of a relatively short maturity for use in meeting the Treasury's immediate financing needs.

Chairman Martin also said that the Board of Governors had been thinking in terms of meeting a portion of the need for additional reserve funds during the last of this year by a reduction in member bank reserve requirements. His own preference, the Chairman said, would be that the Treasury offer securities which would obtain $6 billion in new money at this time, adding that this was only a figure for discussion, that the question of debt management was one for the Treasury to decide, and that he was not thinking of any formal suggestion. Chairman Martin then asked for Mr. Sproul's views on the suggestion made by Mr. Leach as well as on the possibility of a reduction in reserve requirements, adding that Mr. Burgess was coming over to lunch this noon and that he might then be able to give the members of the executive committee his latest thinking on the program the Treasury had in mind.

Mr. Sproul then made a statement substantially as follows:

1. Present open market policy is directed toward avoiding deflationary tendencies without encouraging a renewal of inflationary developments. It involves a judgment that the boom has at least levelled off, and that it may have started to wane, despite the continued strength of various statistical indicators.

2. Implementation of such a policy will require the provision of a large amount of reserve funds to the market, during the remainder of the year, to meet some growth factor, seasonal private needs, and Treasury deficit requirements which the banks will have to finance as investors and underwriters. (The figure of $3 billion has been mentioned.)

3. The objective will be achieved if this combination of demands can be met without intensification of the credit stringency which had developed at the beginning of the second quarter (before the present temporary period of abnormal ease), and without flooding the market with reserve funds so that, in effect, an easy money policy will have been established prematurely.

4. The immediate problems are:

(a) To offset, in part, the effect on bank reserves of the elimination of the Treasury overdraft, the decline in float after the mid-month peak, and the increase in currency circulation at the month-end. With some allowance for a reduction in present excess reserves, and for some increase in bank borrowing and in repurchase agreements, this might call for about $200 to $300 million or more of open market purchases each week during the next two statement weeks.

(b) To provide the reserves which will make possible, and successful, the necessitous borrowing of the Treasury. The minimum amount the Treasury will have to borrow to meet its July needs (in addition to the $500 million still to come in through increased regular weekly bill offerings) is about $3 billion; to get through July and August it would need about $4 billion; to have ample funds to carry into early October it might need $5 or $6 billion.

5. We are going to have to put large amounts of reserve funds into the market during the next several weeks, and we are going to have to do it,primarily, so that it will be possible for the banks to meet Treasury needs or, if we prefer, to prevent Treasury needs from upsetting System credit policy. Our purpose should be to do this in the most effective way possible, both from the standpoint of credit policy and debt management. It is not a question of free markets or rigged markets. Whether we operate only in bills, or whether we operate in other short-term securities, it is going to be our operations which will largely determine the cost and almost wholly determine the success of the Treasury's financing.

6. If the Treasury should decide to do its new money borrowing with a further increase in Treasury bill issues, however devised, open market operations in bills would, of course, be indicated. If the Treasury decides to do its financing with a certificate or note, it is my opinion that a much better job could be done if we authorized the Manager of the Account to deal in other short term securities, as well as in bills. From the standpoint of credit policy, we would run less risk of having to flood the market with reserves, in order to float the issue, if we could operate directly at the pressure points, instead of relying on an imperfect market to do the job for us. From the standpoint of debt management, provision of reserves in this way would be most likely to make for a successful offering, and prepare the ground for later heavy refunding operations.

7. The critical point in all this analysis is whether the market is going to expect further significant increases in interest rates and further declines in security prices during the remainder of the year. If System actions do not quickly dispel such expectations, our present credit policy is going to fail and the Treasury's debt management problems are going to be almost insuperable. To confine open market operations to Treasury bills in such circumstances may defeat the legitimate aims of credit policy and debt management.

Mr. Sproul went on to say that his suggestions would leave to the Treasury the question as to how it would finance its needs and would leave to the Federal Open Market Committee the question of how it would operate in the light of the Treasury's financing program. The proposal outlined by Mr. Leach might solve the Treasury problem on the assumption that it would be extremely difficult if not almost impossible to fix a coupon on an offering of Treasury certificates, Mr. Sproul said, but such an assumption would depend on whether the market expected a further increase in yields on Government securities. If the market is not provided with needed reserves, it is likely that each new issue of bills will go at a higher rate which eventually would mean another adjustment in the whole interest rate structure. Mr. Sproul suggested that confusion in the market might be dispelled if, by fixing a coupon on a certificate or note rather than by relying on auctioning of bills, the Treasury indicated its confidence that reserves would be provided. With respect to the amount, Mr. Sproul doubted the desirability of the Treasury's going to the market for $6 billion at this time. He felt it was not necessary to "clear the decks" in order to end the confusion in the market; that that could be done in other ways. To ask the market (which in this case means the banks) to finance a very large amount of new money, which would call for a very large amount of reserve funds, would be coming to the market at a most difficult time. Mr. Sproul felt that other alternatives included the possibility of getting $800 to a $1,000 million through an offering of tax anticipation bills due in December, the offering to be made as quickly as possible and to be supplemented by a short note for whatever additional amount the Treasury needed to carry it to September 15, or by a certificate such as that suggested by the American Bankers Association. Mr. Sproul noted that there is congestion in the maturity schedule from January to June 1954 and that the banks have large portfolios of securities maturing in this period. While it would involve the problem of pricing, Mr. Sproul said, it might be possible in addition to the tax anticipation bills to offer a 14-month note due in September 1954 at around 2-3/4 per cent interest. In sum, his conclusion was that if the System is going to operate only in bills he would think the Treasury should ask for only the minimum amount needed at this time and should get it with the shortest maturity possible. If the System is going to operate in other short-term maturities he would favor a larger amount and the Treasury might consider an eight-month certificate, a 14-month note, or the December tax anticipation bills, or a combination of these. There would be, however, only two offerings, namely, tax anticipation bills to be issued immediately, due in

December 1953, in the amount of $800 to $1,000 million, and whatever other amount was to be obtained by whatever means the Treasury decided upon.

Chairman Martin said that he felt it important that the Treasury clear the decks at this time by an offering of $5 to $6 billion, either by something along the lines Mr. Leach had suggested or the proposal of the American Bankers Association group. He noted that his thinking and that of the members of the Board of Governors who were on the executive committee was in basic disagreement with the views expressed by Mr. Sproul on the matter of operations in bills. The more he thought of it, Chairman Martin said, the more he felt that if the committee were to start operating in intermediate - or longer-term securities, it would be taking a step backward from the free market concept. As to the Treasury financing, Chairman Martin said that if the Treasury announced an issue of $5 billion or more it might be desirable for the Board of Governors to reduce reserve requirements as a means of freeing reserve funds which would help meet the seasonal needs that would take place during the rest of this year for additional credit for normal economic activity and as a means of giving assurance to the banks that such reserves would be available so that they would be in a position to know how to treat the Treasury financing offer.

Chairman Martin then called upon Mr. Youngdahl for a discussion of possible changes in reserve requirements. Mr. Youngdahl referred to a tabulation, copies of which were distributed, indicating probable changes in factors affecting demand for Federal Reserve Bank credit during the next several weeks as well as estimated member bank reserve positions under various assumptions as to Treasury financing and Federal Reserve credit actions. Mr. Youngdahl emphasized that there was no implied recommendation in the figures he presented, that they merely indicated the probable reserve position of member banks during the next several weeks, including their position in the event reserve requirements were lowered by various amounts indicated. Mr. Youngdahl noted that if reserve requirements were reduced during the first half of July so as to provide around a billion dollars in reserve funds, and if open market operations continued to supply funds to the market on a fair scale, there would still be substantial borrowing by member banks, probably in the neighborhood of $500 million, which he felt would be as restrictive in its influence as had been borrowings of $1-1/4 to $1-1/2 billion some months ago.

Chairman Martin said that it was a question of what was the best way out of the present situation. As Mr. Sproul had indicated, the Federal Open Market Committee at its meeting on June 11 agreed that operations should be carried on with a view, among other things, to avoiding deflationary tendencies without encouraging a renewal of inflationary developments. It was clearly the Committee's objective to avoid having the economy move sharply in either direction. Any action that might be taken, he said, would be subject to misinterpretation, but reserve requirements are relatively high at present and the suggested reduction by the Board of Governors would be one way of putting reserves into the market quickly, letting the market adjust as it would. While some might interpret this as a decision on the part of the Federal Reserve that major adjustments in the economy were impending, on the other hand the amount of reserves it was proposed to release was not very large, and any other action taken might raise questions of the same nature. Also, much the same problem would be presented whether action was taken now or whether it was delayed until there was evidence of an actual down turn in the economy.

In response to a question from Mr. Vardaman, Mr. Sproul stated that if the Treasury financing were to be in the form of certificates, he felt the System account should extend its operations to that area of the market also; operations would still be in short-term securities, and at present he would not contemplate any operations in longer-term securities. If the Board were to reduce reserve requirements, Mr. Sproul said, the necessity for operating in short-term securities other than bills would be lessened. If reserve requirements were to be reduced, Mr. Sproul felt that the effects of the action should be directed most heavily toward the banks which could be expected to take up most of the Treasury financing, which would indicate that the greater reduction should be in central reserve and reserve cities rather than in country banks. This also would indicate that the reduction should apply to demand deposits only.

Mr. Erickson said, in response to a question from Chairman Martin, that he had not given a great deal of consideration to the possibility of a reduction in reserve requirements but that the only objection to such action under present circumstances that occurred to him was the psychological effect it might have in indicating that the Federal Reserve System had changed its credit policy and now anticipated an early down turn. As to the amount of Treasury financing, Mr. Erickson leaned toward a $6 billion offering promptly and toward the use of additional weekly issues of bills along the lines suggested by Mr. Leach. On the other hand, if the Treasury should go to the market with certificates, although he would still prefer to confine System operations to bills, it might then be desirable as Mr. Sproul suggested to authorize some operations in other short-term securities. Mr. Erickson felt that if reserve requirements were to be reduced the reduction should apply across the board on demand deposits, probably with 2 per cent in central reserve cities and 1 per cent in all others.

There followed a general discussion of the possible desirability of a reduction in reserve requirements during which Mr. Vardaman indicated that he was in favor of such a reduction but that he would prefer that it apply to time deposits as well as to demand deposits. He emphasized that the reduction should be made equal for all member banks regardless of geographical location.

Mr. Mills noted that if such a reduction extended to time deposits it would aggravate the possibility of country banks coming into a larger amount of the reserves that would be released than was appropriate for the economy; he would not wish to see such a reduction apply to time deposits at this time.

Mr. Sproul said that one reason for his reluctance to see reserve requirements reduced has been that it would get the Board into the position of using reserve requirements in the tactical area rather than keeping the use of such an instrument for broad fundamental strategy purposes, to which he felt adjustments in reserve requirements should be limited. Mr. Sproul felt that the magnitude of the existing problem might be exaggerated by the figures Mr. Youngdahl had presented, in that a limit of $200 million a week for purchases of bills for the System account, that had been a feasible limit in the last two or three weeks would not be the limit that would be feasible during the next two or three weeks, and that member bank borrowing might well go above the level of $500 million mentioned by Mr. Youngdahl without being unduly restrictive.

In the course of the discussion, Chairman Martin stated that one of the problems facing the committee was the fact that early in May the money market had gotten into a knot. He would not go so far as to say that the economy is now cresting, as had been indicated in Mr. Earhart's statement at the meeting of the full Committee on June 11, but he felt it probably was closer to that point than it had been earlier. But at all times it was important to avoid financial stringency such as might result if a sufficient number of financial knots got to working in the financial mechanism across the country. Chairman Martin felt that there would be some misinterpretations of a substantial reduction in reserve requirements which would be rather unfortunate, but any action taken would be subject to misinterpretation: open market operations would be misconstrued, the discount rate was in a position that did not fit into the market and action taken to bring it into line with the market would be misconstrued. All in all, Chairman Martin felt that a strong case could be made for reducing reserve requirements and he leaned in the direction of doing so, particularly if the Treasury were to proceed in its financing to clear the decks by a minimum issue of $5 billion. Chairman Martin stated that while he did not expect the executive committee to reach any conclusion as to either the Treasury financing or member bank reserve requirements, he would like to know whether there was any disagreement with the view that it would be desirable for the Treasury to offer a large issue, say $5 billion or more, in order to get its financing out of the way for the next two to three months.

Mr. Sproul questioned whether it was desirable, and said that such action would magnify, perhaps unnecessarily, the problem of providing reserves. Smaller financing which would not require that such a large amount of reserves be put into the market might be preferable to putting more reserves into the market at this time when the System was still trying to walk the tightrope between inflationary and deflationary developments. The most important question in the market, Mr. Sproul said, was whether the reserves were going to be available to see the Treasury through this financing period. While the System's actions in the last few weeks had helped to clarify the answer to this question, he felt it needed further clarification in the next two or three weeks.

Mr. Erickson stated that he would prefer to see the Treasury clear the decks and get the full $5 or $6 billion that apparently would be needed during July and August.

Mr. Mills, in referring to Mr. Sproul's earlier comment, expressed the view that if the Federal Reserve extended its operations beyond bills into other short-term obligations, that action, combined with the Treasury's large financing operation, would of itself disconcert the market and would make it appear that the System had some ulterior motive and was scattering its shots by placing funds in other than the shortest term securities. He felt strongly that there should be a reduction in reserve requirements and that the System should confine its operations to the buying of bills. Such actions--reduction in reserve requirements and continued aggressive purchases of bills--would amount to notifying the market that the System was meeting the Treasury's needs and was laying a basis for assuring that, as the autumn season developed, funds would be available through the discount window or through open market operations to meet the economy's needs as they revealed themselves.

Mr. Sproul said that he agreed with Mr. Mills to the extent that if the Treasury is to go to the market for $5 or $6 billion, the System would be forced to lower reserve requirements.

Chairman Martin again expressed the view that it would be preferable for the Treasury to clear the decks at this stage, and he emphasized his belief that at all times the Federal Reserve should direct its operations to avoid developments of financial knots.

Mr. Szymczak recalled that years ago the Federal Open Market Committee had moved gradually into the orderly market concept, from which it moved almost imperceptibly to a fixed peg on Government securities that lasted for years. He felt that if it again got started in the direction of buying Government securities other than bills, it was only a question of time until it would be right back with the peg.

Mr. Sproul did not share this feeling; he felt that the committee need not take that course, and said that his recollection of past experience did not coincide with Mr. Szymczak's and that the only time operations need be conducted in other than bills would be when such operations fitted into monetary policy.

Chairman Martin suggested that the committee consider the instructions to be given to the Federal Reserve Bank of New York, noting that any actions which might be taken at this time would be without knowledge of the Treasury's specific financing program.

> Mr. Mills moved that the executive committee instruct the management of the System open market account to continue the present program of purchasing Treasury bills for the purpose of aggressively supplying reserves to the market, in accordance with the directive issued by the executive committee to the Federal Reserve Bank of New York at its meeting on June 11, 1953, with the understanding that purchases would be limited to bills. In making his motion, Mr. Mills noted that purchases of bills recently had been at the rate of $200 to $300 million a week.

Mr. Sproul felt that it would be unfortunate to fix any specific figures of the amount of purchases to be made for the System account. He also felt that if the Treasury were to decide to do its financing with a certificate or a note the executive committee would be well advised to give the management of the System account discretion to operate in that area of the market as well as in Treasury bills in order to give flexibility.

Mr. Szymczak stated that he would prefer to operate in bills because they are not a coupon security and because as soon as the committee started purchases of coupon securities it would move in the direction of fixing the rate on such securities.

Mr. Sproul said that the amount the committee put into bills and the speed with which it did it would determine the rate at which the Treasury would do its financing, just as much as would the purchase of coupon securities. Also, if the Board of Governors reduced reserve requirements, it would be determining the rate at which the Treasury could do its financing. He felt that there were three alternatives to be considered: (a) If the Treasury were to clear the decks with a $5 to $6 billion financing it would be wise for the Board of Governors to reduce reserve requirements in order to carry out System policy. (b) If the Treasury should decide to borrow a smaller amount, say $3 to $4 billion, and to issue a certificate or a note, it was Mr. Sproul's view that the management of the account should be authorized to operate in short-term securities other than bills. (c) If the Treasury should decide to do its financing with a series of additional bill offerings along the lines discussed earlier in the meeting, open market operations in bills would be indicated.

Mr. Mills said that under any of the proposals discussed by Mr. Sproul it would be essential to continue the bill buying program at at least the present level. He felt that the committee could act on this assumption with the understanding that if the discussion with Mr. Burgess appeared to make it desirable to do so, the meeting could be reconvened following luncheon.

Chairman Martin said that it appeared to be the consensus that the current program of bill purchases should be continued in carrying out the general policy of the Federal Open Market Committee, and Mr. Sproul stated that there was no question in his mind as to the necessity for this procedure, that the committee should aggressively acquire bills in the near future.

The meeting then recessed for luncheon and reconvened at 2:15 p.m. with Messrs. Martin, Sproul, Erickson, Mills, Szymczak, Robertson, and Riefler present.

Chairman Martin referred to Mr. Mills' motion that the executive committee instruct the Manager of the System Open Market Account to continue the present program of purchasing Treasury bills for the purpose of aggressively supplying reserves to the market with the understanding that operations would be limited to bills, and to the subsequent discussion of that motion, of Treasury financing needs, and of the possibility of a reduction in reserve requirements of member banks.

Mr. Sproul stated that in view of the probability that the proposal for a reduction in reserve requirements of member banks would be adopted, the urgency of the need to restore greater discretion to the Manager of the System Open Market Account to effect transactions in short-term securities other than bills was lessened. He still felt, however, that it was very desirable that the Manager of the System Account have authority along the lines he had suggested; he did not know what kinds of situations might arise to make the use of such authority important in carrying out credit policy, and if the executive committee did not wish to give such authority to the Manager of the Account, Mr. Sproul felt that it should at least authorize transactions in short-term securities other than bills for the System account subject to consultation with respect to such transactions with the Chairman of the executive committee.

Mr. Mills stated that he still felt it was desirable to limit the authority for operations in the System account to transactions in bills, although the management of the account should always feel that it could approach the executive committee at any time with suggestions for a modification in the authority. This, he said, seemed to him to provide ample leeway within which operations of the System account might be carried on.

Mr. Sproul reiterated his view that such authority might not be adequate, that a situation might arise which required quicker action than could be obtained if it were necessary to communicate with all members of the executive committee and to convince them of the need for an action which had proved so controversial as this one.

Mr. Szymczak stated that he did not feel it would be desirable to give the management of the System account authority along the lines suggested by Mr. Sproul, that it was his view that transactions for the System account should be limited to Treasury bills.

Chairman Martin said that he had not changed the view which he had expressed at the morning session, namely that transactions for the System account should be limited to Treasury bills.

Mr. Erickson stated that under all the circumstances he would prefer to try to carry on operations through transactions in bills.

Thereupon, Mr. Mills' motion was put by the Chair and carried, Messrs. Martin, Erickson, Mills, and Szymczak voting "aye", and Mr. Sproul voting "no".

Mr. Sproul suggested that it would be desirable to increase the limitation in the first paragraph of the directive to be issued to the Federal Reserve Bank of New York to $1.5 billion from the present figure of $1 billion, and to continue for the present the limitation of $1.5 billion in connection with the purchase direct from the Treasury of special short-term certificates of indebtedness even though it was anticipated that the Treasury shortly would reduce or pay off entirely such certificates.

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 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 avoiding deflationary tendencies without encouraging a renewal of inflationary developments (which in the near future will require aggressive supplying of reserves to the market), and (c) to the practical administration of the account; provided that the total amount of securities in the System account (including commitments for the purchase or sale of securities for the account) at the close of this date shall not be increased or decreased by more than $1.5 billion;

(2) 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 $1.5 billion.

It was agreed that the next meeting of the executive committee would be called for 10:30 a.m. on Tuesday, July 7, 1953.

Thereupon the meeting adjourned.

Winfield W. Riefler
Secretary