

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 Tuesday, June 8, 1954, at 10:45 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Sproul, Vice Chairman
Mr. Robertson
Mr. Szymczak
Mr. Williams

Mr. Mills, Member of the Federal Open Market Committee

Mr. Riefler, Secretary
Mr. Thurston, Assistant Secretary
Mr. Solomon, Assistant General Counsel
Mr. Thomas, Economist
Mr. R. A. Young, Associate Economist
Mr. Rouse, Manager, System Open Market Account
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. Roosa, Assistant Vice President, Federal Reserve Bank of New York

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 open market operations during the period May 26 to June 3, 1954, inclusive, and at this meeting there was distributed a supplemental report covering June 4 to June 7, 1954, inclusive. Mr. Rouse commented briefly on the 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, transactions in the System account during the period May 26 to June 7, 1954, inclusive, were approved, ratified, and confirmed.

6/8/54

-2-

Mr. Young made a statement with respect to the economic situation pointing out recent developments as summarized in a staff memorandum sent to committee members under date of June 4, 1954. Mr. Young said that the general economic situation appeared to be slightly better than a month ago, if only because activity was definitely no lower than in April or March and was possibly slightly higher. On the favorable side, Mr. Young cited maintenance of the Board's index of industrial production at the level of 123 for April, the same as in March, and the strong possibility that the index for May would slightly exceed the March-April level in view of improvement in output in textiles and steel. Among less favorable pieces of evidence Mr. Young noted reports of larger decline than had been reported earlier for anticipated business outlays for plant and equipment for the third quarter and a further reduction in manufacturing employment in May. There was also less than the seasonal decline in unemployment in May and a further small decline in total personal income in April. Mr. Young noted that there had apparently been a halt in the early-year decline in consumer credit outstanding, while there had been continued general stability of prices, a further reduction in Federal outlays for national security purposes, the maintenance (on a seasonally adjusted basis) of the privately held money supply, and the persistent rise in common stock prices in the face of lower profits and business activity. Mr. Young felt that it was not clear at this time whether the economy had reached a turning point or whether the halt in the decline represented a leveling off, to be followed by further decline later on.

6/8/54

-3-

Mr. Thomas stated that the Treasury's cash balance was expected to rise to about \$5 billion at the end of June. By allowing the cash balance to decline to around \$3 billion in July, the Treasury could probably postpone cash borrowing until August. Borrowing of about \$4 billion in August and September could be accomplished so as to maintain a working balance and yet remain within the statutory debt limitation of \$275 billion until October. A cash deficit of about \$1 billion was anticipated for fiscal 1954, Mr. Thomas said, receipts on a cash basis now being estimated at \$71.5 billion and outgo at \$72.5 billion. Receipts would be about the same as in fiscal 1953 and expenditures about \$4 billion below fiscal 1953. Mr. Thomas said that if the budget estimates for fiscal 1955 were borne out, expenditures would be \$2 or \$3 billion less than in fiscal 1954.

Mr. Thomas commented upon developments in the capital markets, noting that State and local Government securities offerings for new capital during June were likely to be at the record level of \$800 million and that corporate securities offerings were expected to total \$725 million. In the bank credit area, business loans recently have declined further, but banks have increased their holdings of Government securities. Demand deposit and currency holdings have also declined, but no more than seasonally during the period January to May 1954. Member bank reserve positions continued generally easy in May with free reserves fluctuating around \$600 million. The reserve position of banks tightened considerably toward the end of May and early in June, Mr.

6/8/54

-4-

Thomas said, due largely to absorption of reserves through the month end and Memorial Day currency outflows and to some increase in Treasury and other deposits at the Reserve Banks. Looking ahead to the need for bank reserves, Mr. Thomas commented upon a tabulation showing an estimated pattern of reserve changes by weeks from the beginning of June to the end of August, stating that it would appear on the basis of these estimates that the reserve position of banks would remain fairly easy through the week of June 23 but then there would be a sharp drop in free reserves, primarily because of the increase in required reserves, a decline in float, and an increase in currency circulation toward the end of the month. Reserve developments in July and August would largely depend on the timing and amount of Treasury borrowing of new money during the summer months. Figures were presented showing the prospective reserve position of banks under different alternatives.

Chairman Martin commented that the committee might be faced with problems in terms of its policy of active ease, and he suggested a full discussion of all aspects of the situation (including open market operations, discount rate, and reserve requirements) as they related to the policy of active ease. In starting the discussion, he inquired whether there was any feeling that there should be a change in the policy of active ease or in the method of making that policy effective.

Mr. Mills stated that developments of the past two weeks had only strengthened his conviction that the level of free reserves should be maintained above the current volume. He outlined the considerations which

6/8/54

-5-

would lead him to this conclusion and reiterated views expressed at the preceding meeting of the executive committee to the effect that he felt the level of free reserves should be maintained in the \$700-800 million range.

In response to a question from Chairman Martin as to what the securities market was expecting regarding Federal Reserve policy, Mr. Rouse said that comments of securities dealers indicated there was concern whether developments in the international situation or the business situation might bring a change in Federal Reserve policy. There was no question as to the availability of reserves for the present, the concern being whether the economy might go into a war situation. During May, some of the dealers who were carrying inventories of new issues of securities were hoping something might be done to "bail them out".

Mr. Sproul then made a statement substantially as follows:

1. Economic conditions and the business and credit outlook indicate that current Federal Reserve policy should continue to be one of "active ease".
2. The overall financial and credit situation would appear to be satisfactory. Bank credit is continuously and readily available at moderate rates. Private and local government capital demands have remained strong, the demand for mortgage credit is at record levels, and these demands have been met without strain. The appearance of temporary congestion in the corporate and municipal securities markets seems to have been due to some misjudgment of the volume of public and revenue issues coming forward, and of the prices necessary to move new issues. Speculative anticipation of a reduction in reserve requirements has played a role in the latter area, since a reduction in reserve requirements, prior to need, would be taken as indicating an intention to flood the market with funds, which temporarily would assist the flotation of new issues. Issues priced to yield above 3 per cent have moved readily--the investment funds are there.

6/8/54

-6-

Meanwhile underwriters with sticky over-priced issues have been able to carry their participations, with a profit on the carry, and this fact, plus speculation on a reduction in reserve requirements, has led to some tardiness in breaking up syndicates and in re-pricing and moving securities. It has not been and is not a situation which should or could be remedied by raising our targets of excess reserves and free reserves by a 100 or 200 million, and it is not a situation which can properly be cured by more excessive doses of reserves, which, except temporarily, might even have a reverse effect.

3. The Treasury's cash outlook has changed little in recent weeks, and it does not appear that Treasury operations will raise serious problems for credit policy during June. The amount of new money needed by the Treasury during the last half of the calendar year still seems to be about \$10 billion. The Treasury can probably get through July without borrowing, but will need new money early in August and borrowing of, say \$5 billion, announced in July with a payment date early in August is indicated, if possible under the debt limit. A tax anticipation certificate (March - June 1955) seems likely, with decision on intermediate or long-term financing postponed until fall. (There is also the August-September refundings to be considered--7.5 billion).
4. A considerable part of this July-August new money financing will have to be carried, at least initially, by the banks and in addition a seasonal increase in bank loans may be anticipated to begin in July.
5. A major portion of these needs could be met by a decrease in reserve requirements, geared closely to the amount and timing of the Treasury's summer financing, as perhaps the easiest way to meet a need of the magnitude indicated and to maintain existing credit policy.
6. Meanwhile, with open market purchases of \$175 million during the current statement week, present projections indicate no need for further action to supply reserves until the week ending June 30. There are expected to be substantial reserve losses during the week and the first two days (July 1 and 2) of the following statement week. Outright purchases to meet part of the end of June - beginning of July need would seem to be in order, if Treasury bills are available, supplemented by temporary additions to market funds through repurchase

6/8/54

-7-

agreements. The June 30 like the December 31 squeeze would be an appropriate time to use the repurchase method of supplying some reserves, and it would have the further advantage of not loading up the System portfolio too heavily prior to a decrease in reserve requirements. If the repurchase route is to be opened, however, a temporary reduction in repurchase rates, perhaps to 1 per cent, will probably be necessary.

7. A reduction in reserve requirements could then be announced about mid-July, the actual dates of the reductions to coincide closely with the payment date of the Treasury financing. A reduction at central reserve and reserve city banks might be scheduled in two steps, on the last statement date in July and the first statement date in August, and at "country" banks on August 1.
8. If the practical reduction in reserve requirements puts more funds into the market than are needed to maintain the policy of "active ease" as it has been maintained, surplus funds could be withdrawn through redemptions and sales of Treasury bills by the System Account.

Mr. Williams stated that there was a vigorous discussion of conditions in the Treasury bill market at the last meeting of the Board of Directors of the Federal Reserve Bank of Philadelphia at which time one of the banker members expressed the view that it was not desirable for the Federal Open Market Committee to follow the policy of confining its operations to the short end of the market.

Mr. Robertson expressed general agreement with most of the points mentioned by Mr. Sproul. His feeling was that the degree of ease that had resulted from the committee's operations recently had been about as nearly "right" as the committee could expect to get it. To make the situation any easier would merely drive the bill rate down further. With respect to Mr. Sproul's comments on reserve requirements, Mr. Robertson suggested that it might be possible to provide funds that would be needed toward the end of June through a reduction of around \$300 million in reserve requirements against time deposits. Mr. Robertson felt that such

6/8/54

-8-

an action would not be upsetting to the market, that it would provide almost no reserves to central reserve city banks, and that it would fit in with the situation where new issues were coming into the market and country banks would be purchasing them. In addition, Mr. Robertson thought that the Federal Reserve might use repurchase agreements to some extent toward the end of June. Otherwise, for the next two weeks he would be inclined to follow about the degree of ease that the committee had tried to attain in the recent past.

Chairman Martin inquired of Mr. Sproul as to his suggestions on reserve requirements, and Mr. Sproul responded that it seemed to him a reduction might better be geared to Treasury financing operations rather than to a move to encourage country banks to take up new municipal or other issues of securities.

Mr. Szymczak stated that he would make no change in the discount rate at this time. He felt that by the time of the full Committee meeting to be held later this month, the committee would know more about the Treasury's needs and the extent to which increased reserves might be required for that and other purposes. As far as the open market was concerned, Mr. Szymczak thought that additional reserves need not be supplied during the period of the next two weeks. He also felt that it was important that the rate on repurchase agreements be reduced.

Chairman Martin expressed the view that the sense of the meeting was that operations for the System account during the next two weeks should continue just about as during the past two weeks, and he stated

6/8/54

-9-

that if there was no disagreement this would be considered as the program to be followed until the next meeting.

No disagreement with this suggestion was indicated.

Mr. Rouse stated that he had no suggestion for change in the directive to be issued 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 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 promoting growth and stability in the economy by actively maintaining a condition of ease in the money 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 \$500 million;

(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 \$500 million;

6/8/54

-10-

(3) To sell direct to the Treasury from the System account for gold certificates such amounts of Treasury securities maturing within one year as may be necessary from time to time for the accommodation of the Treasury; provided that the total amount of such securities so sold shall not exceed in the aggregate \$500 million face amount, and such sales shall be made as nearly as may be practicable at the prices currently quoted in the open market.

Chairman Martin then referred to the discussion at the meeting of the executive committee on March 30, 1954, of memoranda relating to bankers' acceptances, including staff proposals regarding steps the Federal Reserve might take to assist in bringing about a more freely functioning bankers' acceptance market. He suggested that in view of the understanding that this matter would be placed on the agenda for the next meeting of the full Committee to be held on June 23, there be further discussion of it at this time.

Mr. Sproul said that he did not feel the proposals regarding bankers' acceptances were of major importance at the present time but that they did have considerable importance in the re-establishment of a more effective procedure for financing international trade. If it were desired that this country and the New York market develop further in the financing of international trade so that some of the burden might be taken off the London market, it would seem desirable, Mr. Sproul said, to bring about some greater flexibility in the acceptance market, both in terms of getting bills into the market and in terms of getting away from rigidly administered rates and having an instrument which responded more readily to market conditions. Mr. Sproul felt

6/8/54

-11-

that the Federal Reserve System could be of assistance by showing greater flexibility in its own rates on bankers' acceptances and allowing the System account to buy some bills from time to time.

Mr. Robertson recalled that when bank acceptances were discussed earlier this year he raised some questions regarding their use and that, with the approval of the Board of Governors, he had requested Mr. Hexter, Assistant General Counsel of the Board, and Mr. Youngdahl to make a survey regarding present conditions and practices in that market, as a part of which they visited New York for the purpose of obtaining first-hand information. He stated that Messrs. Hexter and Youngdahl had prepared a factual memorandum dated May 14, 1954 and suggested that copies of that memorandum be sent to all members of the Federal Open Market Committee along with the staff memoranda dated March 24 and 25, 1954 (discussed by the executive committee on March 30, 1954) giving background information on the role of bankers' acceptances and containing the staff proposals for action to bring about a more freely functioning market. Mr. Robertson went on to say that as a result of the study he had given the matter, he also had prepared a memorandum raising some question as to the staff proposals. After reading this memorandum dated June 1, 1954, Mr. Robertson suggested that copies of it also be sent to the members of the Open Market Committee and the other Reserve Bank Presidents prior to discussion of the subject at the meeting to be held on June 23.

It was agreed that copies of the four memoranda referred to relating to bank acceptances should be sent to all members of

6/8/54

-12-

the Federal Open Market Committee and to the Reserve Bank Presidents who are not currently members of the Committee for discussion at the meeting of the full Committee to be held on June 23, 1954. In taking this action, it was understood that additional memoranda would be prepared by Messrs. Riefler and Rouse commenting further on the subject and would be given similar distribution.

Mr. Robertson stated that he had discussed with Mr. Rouse the matter of eliminating the one-day lag which takes place between purchases for the System open market account and actual payment for such securities, and that Mr. Rouse had sent him some material which had been prepared at the Federal Reserve Bank of New York giving information concerning this matter. He inquired of Mr. Rouse whether it would be possible to obtain more information as to the practicability and desirability of changing the procedure in connection with purchases for the System account so that funds resulting from such purchases would be injected into the market on the day the orders were placed.

Mr. Rouse suggested that the approach to the question be from the standpoint that elimination of the lag might be desirable, and material prepared with a view to finding out how it might be accomplished. It was understood that Mr. Rouse would undertake to prepare such additional information.

It was agreed that the next meeting of the executive committee would be held on Wednesday, June 23, 1954, following the meeting of the Federal Open Market Committee to be held that day.

Thereupon the meeting adjourned.


Winfield W. Riefler