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, November 23, 1954, at 10:45 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Robertson
Mr. Szymczak
Mr. Williams
Mr. C. S. Young, Alternate for Mr. Sproul

Messrs. Balderston and Mills, Members of the Federal Open Market Committee

Mr. Riefler, Secretary
Mr. Thurston, Assistant Secretary
Mr. Vest, General Counsel
Mr. Thomas, Economist
Messrs. Bopp and Ralph A. Young, Associate Economists
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. D. C. Miller, Economist, Division of Research and Statistics, Board of Governors
Mr. Gaines, Securities Department, Federal Reserve Bank of New York

Before this meeting there had been sent to the members of the committee a report of open market operations covering the period November 9, 1954, through November 18, 1954, inclusive, and at this meeting there was distributed a supplementary report covering commitments November 19-22, inclusive. Copies of both reports have been placed in the files of the Federal Open Market Committee.

Mr. Rouse stated that there had been a delay in the expected tightening of the reserve position of New York City banks and for the past few days free reserves had been running around $200 million higher than had been anticipated. He expected some tightening toward the end of this week, however, and stated that, in fact, some evidence of such tightening showed up yesterday. In view of this situation, there had been no open market operations during the past few days pending the meeting of the executive committee today. Mr. Rouse felt that free reserves would average around $700 million for the current statement week even though they might close at a level of $300-400 million.

In response to a question from Mr. Balderston, Mr. Rouse stated that the sale of securities for cash delivery on November 12 had worked out satisfactorily. Mr. Rouse noted that conditions for such a sale were ideal at that time, and he added the comment that it appeared that if transactions for cash delivery were arranged to take place before twelve o'clock noon they would work out satisfactorily, but there was a question as to whether they could be made to work satisfactorily if arranged for later during the day.

> Upon motion duly made and seconded, and by unanimous vote, the open market transactions during the period November 9-22, 1954, inclusive, were approved, ratified, and confirmed.

Mr. Ralph Young presented a report on economic developments in which he brought out the views expressed in the staff memorandum distributed under date of November 19, 1954, namely, that business sentiment and economic opinion generally appear to have become more optimistic recently, and most observers are debating the speed, extent, and duration of a possible rise in activity. The general view seems to be, he said, that recovery is occurring this quarter and that moderate further expansion is probable in early 1955. Very few analysts, however seem to be expecting expansion of sufficient magnitude over the period immediately ahead to restore industrial production or employment to the peak levels reached in 1953. Mr. Young also noted that, with over-all productivity continuing to grow rapidly and with the labor force increasing at about 700,000 a year, return even to the levels of output of mid-1953 would imply levels of unemployment considerably higher than prevailed at that time and appreciably above the seasonally low current levels.

Mr. Thomas then commented on capital market developments, bank credit, and reserves. In connection with his comments, Mr. Thomas presented a sheet showing an estimated pattern of reserve changes during the weeks ending November 17, 1954 - January 5, 1955 which indicated that, without further open market operations by the System, free reserves might range, on a weekly average basis, well below $400 million during the first three statement weeks ending in December, after which they could be expected to rise moderately. Mr. Thomas noted that the return flow of currency following the Christmas holidays would take care of additional needs for reserves at that time and that the problem to be considered at present was what, if any, action should be taken to supply additional reserves during the next two weeks. If it were decided to supply additional reserves, Mr. Thomas felt that any needs might well be met through making available the repurchase facility.

In response to Chairman Martin's inquiry as to how the Treasury's current refinancing had been received, Mr. Rouse stated that, on the basis of comments from banks and dealers, reception of the issues was very good, and that the securities offered had just fitted in with the needs of holders of maturing or called securities. He noted that the books for the new offerings would close on Wednesday night, November 24, and that there would be a good indication by Friday afternoon, November 26, as to how subscriptions had gone, with final figures available next Monday. He estimated that between 60 and 70 per cent of the maturing securities held by commercial banks would be replaced with the new 2-1/2 per cent bond to be due August 15, 1963. Mr. Rouse also stated that dealers had been absorbing such "rights" as had been available in the market.

During Mr. Rouse's comments, Mr. D. C. Miller entered the room.

Chairman Martin commented that the economic and credit review and Mr. Rouse's statement with respect to the Treasury financing provided the setting within which the committee would be operating during the next two weeks. He noted that at the meeting of the executive committee on November 9 he had expressed views with respect to the presence of speculative psychology in the general situation, adding the comment that he had not changed these views substantially since that time. Chairman Martin felt that the committee should not now do anything to cause a disturbance in the Government securities market but that it should be considering whether it could let the forces in the market have greater play than they have had heretofore.

Mr. Szymczak stated that he saw nothing in the economic picture as presented by Mr. Young or in the reserve picture as presented by Mr. Thomas that would require a drastic change in what the committee had been doing. The question was what amount of reserves would be required over the period of the next several weeks. Mr. Szymczak suggested that committee operations to meet these reserve needs between now and the meeting of the full Committee to be held during the week beginning December 6 should be on a day to day basis, and should depend on "feel" of the market.

Mr. C. S. Young stated that banks in the Chicago District, both city and country, generally were planning to take the 2-1/2 per cent Treasury bonds due August 15, 1963 that had been offered in the current refinancing, and that the consensus was that the securities offered fitted in well with the needs of the banks. As to open market operations during the next two weeks, Mr. Young hoped that market forces could have a little greater play than had been the case previously and that any shortness in reserves could be taken up through use of repurchase agreements. At this point, he saw no need for any other operations to affect the market.

Mr. Mills stated that decisions of banks to go so largely into the 2-1/2 per cent Treasury bonds currently offered would effect quite a change in their liquidity position around December 15 and that their reaction to a reduction in the volume of free reserves would depend on how conscious they were of the change in their liquidity. He thought that between now and the meeting of the full Committee banks might need more relief in the form of additional reserves than would be afforded on the basis of projections of reserves, and he questioned whether repurchase agreements should be relied upon to provide all reserves that might be needed although he would certainly favor their use over the year-end. Mr. Mills would be inclined to think that the committee should rely partly on bill purchases in meeting reserve needs in the period just ahead.

Mr. Robertson said that the information presented today verified the views expressed at the preceding meeting regarding the desirability of letting free reserves range lower than had been the case earlier this fall. He felt there should be no change in the program for operations indicated at the November 9 meeting, provided that meant that free reserves were to be permitted to move toward the lower end of the $400-700 million range discussed as a target. Mr. Robertson also stated that if any condition developed which called for additional reserves in the market, he felt that need should be met by means of outright purchases of securities for the System account.

Mr. Balderston said that he had been surprised that the speculative atmosphere stemming from the stock market had not yet shown up in commodities and in inventory accumulation. He felt that the program followed by the committee recently should be continued but that attention should be directed toward stock market activities and that consideration should be given to the possible desirability of action by the Board of Governors to increase margin requirements.

Mr. Williams stated that he saw no reason for a change in the committee's operations at this time and that, as he had indicated at the preceding meeting, any braking action should be very smooth. Mr. Williams also felt that the existing general policy, of having free reserves closer to the lower end of the range, should be continued.

Chairman Martin stated that the general policy as laid down by the full Committee and as carried out by the executive committee in recent months had been virtually to supply almost every deficiency that might develop in reserve needs of the banking system. He noted that a year ago the committee felt that free reserves in the amount of $100 million provided a rather good margin. The general economic outlook seemed to him to be clearly better today than a year ago, the Chairman said, and yet the committee had been supplying funds which resulted in free reserves running to $700 or $800 million during the current Treasury financing and which recently were over a billion dollars. Chairman Martin stated that the committee could not now tell how the volume of free reserves during the next few weeks would turn out as compared with the staff projections, but he felt that, as Mr. Szymczak had put it, it would be necessary for the committee to rely on the Manager of the System Account in a period such as the present, having him base operations on the "feel" of the market, within the limits of the over-all policy. Chairman Martin emphasized the view that, if the committee were to have flexibility in its operations, it should be permitting the forces of the market to operate during this period.

Mr. Williams stated that he interpreted this view to represent the views expressed at the preceding meeting of the committee.

Mr. Rouse said that although Mr. Sproul was unable to attend today's meeting, he had indicated his views in a brief memorandum. Mr. Rouse summarized these views, stating that Mr. Sproul felt that the present prospect was for a rise in economic activity of something more than seasonal proportions continuing into 1955 but, in terms of unemployment, probably not enough increase to offset the rise in productivity and working population. This would not look like a boom or like the stuff from which inflation is made. The action of buyers as reflected in the stability of prices confirmed this sort of forecast. Mr. Sproul had also indicated that there was some evidence of speculative activity in the stock market and in the construction industry, but that it was doubtful if the committee should try to do anything about the former by means of margin controls in the light of the prospective business situation. He felt there was little, if anything, that the committee could do about the situation in the construction industry in the face of the general Government policy on mortgage financing unless it really wanted to tighten credit by quantitative measures. Mr.

Sproul had also indicated that there might be speculation in the automobile industry--speculation as to what the consumer could be pushed into buying by ballyhoo, changed appearance of new models, and easier installment credit. It did not look as though lower prices could be offered in an attempt to broaden the market because of increased labor costs. Mr. Sproul thought that "snubbing up" the general credit situation would still appear to be the best policy. "Snubbing up" would mean a lower level of free reserves and, presumably, short-term money market rates closer to the discount rate.

Chairman Martin stated that he would take it from Mr. Rouse's summary of Mr. Sproul's views that the latter was supporting the general theory of the meeting of the executive committee on November 9, and Mr. Rouse stated that that was correct. Chairman Martin went on to say that it was difficult to know just how to write an instruction regarding open market operations during the next two weeks other than to record in the minutes the views that had been expressed and to give the Manager of the System Account discretion to operate in accordance with these views. Chairman Martin felt it was very clear that the committee had been forcing the market for some time. If it was not going to let the market have some play, it might as well reconcile itself to indefinite expansion of the money supply. Chairman Martin did not think this was of great importance at the immediate moment, although he leaned definitely on the side of permitting the market to tighten up unless something unforeseen developed. This, he said, was a matter of day to day operation. He thought that permitting the natural processes to operate in the market should be the committee's program during the next two weeks, bearing in mind Mr. Mills' point regarding the possible reaction of banks to a reduction in free reserves at a time they were acquiring additional amounts of longer-term Government securities. In a further comment during a discussion of the possible effects on long-term interest yields of a rise in short-term rates to a level closer to the discount rate, Chairman Martin stated that the discussion contemplated retention of ease in the money market but not so much as there had been and not so active.

Mr. Rouse inquired, in the light of the directive from the full Committee, how far the executive committee might go in such a program.

Mr. Szymczak stated that it was a question of what action might be required in the market at the moment, playing by ear, within the terms of the existing directive from the full Committee.

Chairman Martin suggested that, at the forthcoming meeting of the full Committee, tentatively set for 9:30 a.m. on Tuesday, December 7, 1954, consideration should be given to the possibility of changing the over-all directive or at least modifying that part which called for "promoting growth and stability in the economy by actively maintaining a condition of ease in the money market." For example, it might be desirable to modify the directive to call for the promotion of growth in the economy or growth and stability, but to eliminate the reference to "actively maintaining" a condition of ease.

In response to a question from Chairman Martin as to what problems he foresaw in the proposal that the Manager of the System Account be given discretion during the next two weeks to operate along the lines of the foregoing discussion, Mr. Rouse stated that it was difficult to visualize how much activity there would be. There would be a long carry for the dealer market between now and December 15, he said, and in his conversations with dealers yesterday as to whether they were having any difficulty in securing funds to carry Government securities, including carrying "rights" to the new offering, he had received the comment that funds were very freely available. Because of this response, he was more optimistic than he might otherwise have been in view of the length of the carry, but it was entirely likely that with free reserves around a quarter of a billion dollars the committee might run into some pressure for repurchase agreements at 1-1/2 per cent and there might also be pressure on the Treasury bill market.

Replying to Chairman Martin's further inquiry as to what, if any, change in the directive from the executive committee to the New York Bank was needed, Mr. Rouse suggested that paragraph (3) authorizing the sale of not more than $500 million of specified securities from the System account direct to the Treasury for gold certificates be eliminated as not necessary. As to the amounts in paragraphs (1) and (2), he would suggest no change although he felt the limit in paragraph (1) could be reduced to $500 million from the existing figure of $750 million.

Chairman Martin said that he saw no objection to retaining the figure of $750 million, and there was unanimous agreement that the directive be issued to the New York Bank without change in the limits in paragraphs (1) or (2) but that the third paragraph relating to sales of securities for gold certificates be terminated effective immediately.

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 $750 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.

Chairman Martin suggested that consideration of memoranda previously distributed relating to repurchase agreements be carried over until the next meeting, and no objection to this procedure was indicated.

In this connection, Mr. Rouse stated that he saw no need for a lower rate than 1-1/2 per cent on repurchase agreements during the next two weeks, and he suggested that the authorization for a range of 1-1/4 to 1-1/2 per cent on such agreements be eliminated but that authority for the Federal Reserve Banks to enter into repurchase agreements at 1-1/2 per cent, subject to the terms and conditions of the arrangement approved June 24, 1954, be continued.

There was agreement with this suggestion.

Secretary's Note: Pursuant to this action, the following telegram was sent to the Presidents of all Federal Reserve Banks and to the Manager of the System Open Market Account under date of November 23, 1954:

"At a meeting today the executive committee of the Federal Open Market Committee terminated, effective at the close of business today, the authorization to Federal Reserve Banks contained in telegram of November 9, 1954 to enter into repurchase agreements at a range of rates of 1-1/4 per cent to 1-1/2 per cent; and continued, until further action by the committee, authority for Federal Reserve Banks to enter into repurchase agreements at a rate of 1-1/2 per cent, subject to other terms and conditions of the arrangement authorized effective June 24, 1954, pursuant to the action of the full Committee at its meeting on June 23, 1954."

Mr. Rouse then referred to a memorandum prepared at the Federal Reserve Bank of New York under date of November 22, 1954, presenting alternative exchange subscriptions of System holdings of December 15, 1954 Treasury maturities, copies of which were distributed at this meeting. Mr. Rouse stated that he would appreciate guidance as to what procedure should be followed in connection with holdings of Treasury notes and bonds in the System account which were maturing or which had been called for payment December 15, 1954. The amount of the System account holdings was approximately $7,283 million and the outstanding amount of such Treasury securities was $17,347 million.

Following a discussion of the several alternatives presented in the memorandum, it was agreed unanimously that System holdings of December 15 maturities should be exchanged in amounts designed to effect an equal distribution in the System account of August 15, 1955 and December 15, 1955 maturities (1-1/4 and 1-3/4 per cent combined). This would mean subscribing for $4,763 million of the August 1-1/8 per cent certificates and $2,520 million of the December 1-1/4 per cent certificates.

It was agreed that the next meeting of the executive committee would be held on Tuesday, December 7, 1954, following the meeting of the full Committee tentatively scheduled to be held at 9:30 a.m. that day.

Thereupon the meeting adjourned.

Winfield W. Riefler
Secretary