THIRTY-THIRD

ANNUAL REPORT

of the

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

COVERING OPERATIONS FOR THE YEAR

1946

cent bonds maturing on March 15, 1946, would be paid off. These issues were held largely by commercial banks and the Federal Reserve Banks and their retirement would effect a substantial reduction in the volume of bank credit outstanding.

Before this meeting of the Committee, consideration had been given to the question what should be done with respect to the preferential discount rate of ½ per cent in effect at the Federal Reserve Banks on advances to member banks secured by Government obligations, the termination by the Federal Open Market Committee of the ⅜ per cent posted rate at which the Federal Reserve Banks stood ready to purchase Treasury bills offered to them, the policies of the Treasury with respect to management of the public debt including debt retirement, and possible legislation by Congress to increase the powers of the System in the field of credit regulation.

The discontinuance of the preferential discount rate was under active consideration by the Federal Reserve Banks and the Board of Governors and was being discussed with the Treasury at the time of this meeting. It was the belief of the Federal Open Market Committee that the discontinuance of that rate, which was a temporary war measure designed to meet a special situation, should be the first step in a policy which had as its objective the prevention of further expansion of bank reserves and that, for reasons discussed in the annual report of the Board of Governors to which this record is appended, it was important that the large supply of funds resulting from deficit war financing through the banks be reduced rather than increased during the year. The Committee was of the opinion that such reduction could be effected without increasing the cost of carrying the Government debt. It was also felt that until the preferential discount rate was eliminated and the effects of that action on the money market and on yields on Government securities could be observed, and inasmuch as substantial amounts of reserve funds would be required in the market in connection with the retirement of Government debt, the Committee should continue the existing open market policy of maintaining an adequate supply of member bank reserves and at the same time exerting an influence toward the maintenance of conditions in the Government security market that would be satisfactory from the standpoint of Government requirements.

The above direction was adopted for that purpose. It was in the same form as the direction issued at the meeting of the Committee on October 17, 1945, except that the limitation contained in the first paragraph on the amount by which the total securities held in the System account could be changed was raised from 2 billion dollars to 3 billion. The limitation was increased in view of the large transactions in the System account which it was expected would take place before another meeting of the Committee, arising from the needs for reserve funds in connection with the program for retirement of the public debt and the redemption of securities in the System open market account.

June 10, 1946

Members present: Mr. Eccles, Chairman; Mr. Sproul, Vice Chairman; Mr. Szymczak; Mr. Draper; Mr. Evans; Mr. Vardaman; Mr. Leach; Mr. McLarin; Mr. Young; Mr. Clerk.

1. Authority to Effect Transactions in System Account.

Upon motion duly made and seconded, the following direction to the executive committee was approved by unanimous vote:

The executive committee be directed, until otherwise directed by the Federal Open Market Committee, to arrange for such transactions for the System open market account, either in the open market or directly with the Treasury (including purchases, sales, exchanges, replacement of maturing securities, and letting maturities run off without replacement), as may be necessary in the practical administration of the account or for the purpose of maintaining an orderly market in Treasury securities and a general level of prices and yields of Government securities which will support the Treasury issuing rates of ⅞ per cent for one-year certificates and 2½ per cent for 27-year bonds restricted as to ownership; provided that the aggregate amount of securities held in the account at the close of this date [other than (1) bills purchased outright in the market on a discount basis at the rate of ⅜ per cent per annum and bills redeemed at maturity and (2) special short-term certificates of indebtedness purchased from time to time for the temporary accommodation of the Treasury] shall not be increased or decreased by more than 2 billion dollars.

That the executive committee be further directed, until otherwise directed by the Federal Open Market Committee, to arrange for the purchase for the System open market account direct from the Treasury of 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 amount of such certificates held in the account at any one time shall not exceed 1.5 billion dollars.

During the interim since the meeting of the Committee on March 1, 1946, action had been taken by the Federal Reserve Banks and the Board of Governors to discontinue the preferential discount rate of ½ per cent on advances to member banks secured by Government obligations. In announcing the discontinuance of the rate, the Board of Governors stated that it did not favor a higher level of interest rates on Government securities than the Government was then paying. The Treasury had redeemed for cash more than 10 billion dollars of maturing Government securities since the first of the year and it appeared at the time of this meeting that Treasury balances would permit further substantial retirements in the months immediately ahead. This would continue to reduce the volume of bank credit outstanding and to prevent a return of the downward trend in yields on Government securities that had been present earlier in the year.

At this meeting there was further discussion of the steps that might be taken by the Committee to carry out the System credit policies directed, as part of the program of the Government for combating inflation, toward the prevention of a further expansion of bank reserves and at the same time of any increase in the cost of the Government debt. It was felt that the Treasury program for debt retirement made unnecessary at this time any action to discontinue the outstanding direction issued by the Federal Open Market Committee to the Federal Reserve Banks to purchase Treasury bills offered to them at a discount rate of ⅜ per cent per annum. It was also the view of the Committee that in the existing circumstances the policy referred to above could best be implemented by changing the direction issued to the executive committee with respect to transactions in the System account so that such transactions would be for the purpose of maintaining an orderly market in Treasury securities and a general level of prices and yields of Government securities which would support the Treasury issuing rates of ⅞ per cent for one-year certificates and 2½ per cent for 27-year bonds restricted as to ownership.

The limitation in the first paragraph of the new direction was reduced from 3 billion to 2 billion dollars for the reason that, while operations in the System account before another meeting of the Committee, particularly the redemption of securities being retired, would be substantial, it was believed that the lower limitation on the authority to change the amount of securities in the account would be adequate to meet the situation.

October 3, 1946

Members present: Mr. Eccles, Chairman; Mr. Sproul, Vice Chairman; Mr. Ransom; Mr. Draper; Mr. Evans; Mr. Vardaman; Mr. Leach; Mr. McLarin; Mr. Young; Mr. Peyton.

1. Authority to Effect Transactions in System Account.

Upon motion duly made and seconded, the following direction to the executive committee was approved by unanimous vote:

The executive committee be directed, until otherwise directed by the Federal Open Market Committee, to arrange for such transactions for the System open market account, either in the open market or directly with the Treasury (including purchases, sales, exchanges, replacement of maturing securities, and letting maturities run off without replacement), as may be necessary in the practical administration of the account or for the purpose of maintaining an orderly market in Treasury securities and a general level of prices and yields of Government securities which will support the Treasury issuing rates of ⅞ per cent for one-year certificates and 2½ per cent for 27-year bonds restricted as to ownership; provided that the aggregate amount of securities held in the account at the close of this date [other than (1) bills purchased outright in the market on a discount basis at the rate of ⅜ per cent per annum and bills redeemed at maturity and (2) special short-term certificates of indebtedness purchased from time to time for the temporary accommodation of the Treasury] shall not be increased or decreased by more than 2 billion dollars.

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When this meeting was held, there had been no new developments which presented reasons for a change in the policies adopted by the Federal Open Market Committee. The Treasury had continued its program of debt retirement and had redeemed for cash 17.5 billion dollars of Government securities. Further retirements were expected during the remainder of the calendar year and, therefore, the Committee was of the opinion that there was no need at this time for the elimination of the direction to the Federal Reserve Banks to purchase Treasury bills offered to them at a discount rate of ⅜ per cent per annum. Accordingly, for the reasons previously stated, the above direction was issued to continue the existing policies in effect.