

THIRTY-SIXTH

# ANNUAL REPORT

*of the*

BOARD OF GOVERNORS OF THE  
FEDERAL RESERVE SYSTEM



COVERING OPERATIONS FOR  
THE YEAR

1949

from time to time for the temporary accommodation of the Treasury shall not be increased or decreased by more than 3 billion dollars.

The executive committee is 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 total amount of such certificates held in the account at any one time shall not exceed 1.5 billion dollars.

Votes for this action: Messrs. McCabe, Chairman; Sproul, Vice Chairman; Clayton, Draper, Earhart, Eccles, Evans, Gidney, Leach, McLarin, Szymczak, and Vardaman. Votes against this action: none.

By late June the decline in business activity had gone further than had been considered likely at the beginning of the year and there were indications that it would go somewhat further. On the date of this meeting it was clear that Congress would not extend the temporary authority of the Board of Governors to increase reserve requirements of member banks and that the lapse of this authority at the end of June would reduce reserve requirements of member banks by about 800 million dollars and, therefore, would have a substantial easing influence on the money market. It was also clear that Congress would not extend the temporary authority of the Board for the regulation of consumer instalment credit which would result in greater availability of credit in this field.

It was agreed at this meeting that the easing influence of the reduction of 800 million dollars in reserve requirements should be permitted to make itself felt in the market, and that open market operations should be so conducted, in the light of developments after the reduction in reserve requirements became effective on July 1, as to continue the System's policy of monetary ease. The direction set forth above was adopted for that purpose. The only change from the previous direction was in the reference to orderly conditions as distinguished from stable and orderly conditions in the Government security market.

This was a significant change in the direction and grew out of the suggestion that the declines in business activity that had taken place and the credit policy being currently followed by the Federal Reserve System afforded the Federal Open Market Committee an opportunity to adopt a more flexible policy, first with respect to the general business and credit situation, and second, with respect to support of the Government security market. Discussions at this meeting were in the light of further conferences that had been held by representatives of the Committee with the Secretary of the Treasury in which the view was expressed that the time had arrived when the Federal

Open Market Committee should begin to determine its policies on the basis of the general business and credit situation and orderly conditions in the Government security market, without attempting to maintain a relatively fixed pattern of prices and yields on United States Government securities. Under existing conditions, the revised policy contemplated increased availability of reserve funds and some further decline in rates, and in all conditions somewhat freer movements in prices and yields in the Government security market. The members of the Committee were favorable to such a change in existing policy. The statement issued to the press in connection with this change was as follows:

The Federal Open Market Committee, after consultation with the Treasury, announced today that with a view to increasing the supply of funds available in the market to meet the needs of commerce, business, and agriculture it will be the policy of the Committee to direct purchases, sales, and exchanges of Government securities by the Federal Reserve Banks with primary regard to the general business and credit situation. The policy of maintaining orderly conditions in the Government security market and the confidence of investors in Government bonds will be continued. Under present conditions the maintenance of a relatively fixed pattern of rates has the undesirable effect of absorbing reserves from the market at a time when the availability of credit should be increased.

August 5, 1949

**I. Authority to Effect Transactions in System Account.**

The following direction to the executive committee, which was in the same form as the direction issued at the meeting of the Committee on June 28, 1949, was approved.

The executive committee is 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 light of changing economic conditions and the general credit situation of the country, for the practical administration of the account, for the maintenance of orderly conditions in the Government security market, and for the purpose of relating the supply of funds in the market to the needs of commerce and business; provided that the aggregate amount of securities held in the account at the close of this date other than 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 3 billion dollars.

The executive committee is 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 total amount of such certificates held in the account at any one time shall not exceed 1.5 billion dollars.

Votes for this action: Messrs. Sproul, Vice Chairman; Clayton, Draper, Earhart, Eccles, Gidney, Leach, and McLarin. Votes against this action: none.

During July the decline in business activity continued for the eighth consecutive month. The decline had been orderly and, because of supporting factors in the economy with high levels of activity in some segments, had been relatively mild. The outlook was for a continued high level of activity with a likelihood of some moderate increase in the immediate future. It was not clear, however, whether the corrections that had been made had been sufficient to prevent further declines over a longer term period. The indications were that present credit policy should be one of continued monetary ease as one means of encouraging a high level of business activity while at the same time avoiding conditions of such ease as would prevent needed adjustments in the economy or would encourage undue expansion.

At this meeting it was stated that, if the Federal Open Market Committee should be willing to allow the System's holdings of Treasury securities to go into the market in amounts sufficient to absorb the reserves that would be released by a reduction in reserve requirements, the Board of Governors would reduce reserve requirements by two percentage points on demand deposits and possibly one percentage point on time deposits of all member banks, to become effective on various dates in August and September.

It was agreed by members of the Federal Open Market Committee that, in view of the tendency for declining economic activity in the United States, the release of additional funds to banks by the proposed reduction in reserve requirements was desirable. It was recognized, however, that unless banks were supplied with securities for immediate investment of their additional funds, there would be disorderly conditions in the money market and an unnecessarily sharp and largely temporary decline in interest rates. It was felt that sales of short-term securities by the System would provide banks with liquid assets and prevent an undue decline in interest rates without interfering with the major goal of the reserve-requirement reduction, namely, to encourage the extension of credit beneficial to increased production and employment.

Accordingly, the members of the Committee indicated that if the Board of Governors should reduce reserve requirements by the amount proposed

(approximately 1.8 billion dollars) they would act to reduce the System's holdings of securities to offset the released reserves, and that securities would be sold from the System account until transition to the lower reserve requirements had been made so that the reduction would not result in a general further lowering of short-term rates. The above direction was adopted for that purpose and for the further purpose of continuing the System policy of monetary ease.

DECEMBER 13, 1949

#### 1. Increase in Short-Term Rates.

The members of the Federal Open Market Committee, on November 22, 1949, upon recommendation of the executive committee, authorized the purchase and sale of bills and certificates in the market at somewhat lower prices (higher yields) than had recently prevailed. At this meeting this informal action was approved, ratified, and confirmed.

Votes for this action: Messrs. McCabe, Chairman; Sproul, Vice Chairman; Draper, Earhart, Eccles, Gidney, Leach, McLarin, Szymczak, and Vardaman. Votes against this action: none.

Until the middle of November, operations in the System open market account continued to be carried on under the policy of monetary ease adopted at the meeting of August 5, 1949, as one means of restraining further declines in production and employment. However, when the executive committee met on November 18, 1949, there had been a moderate recovery from the lows reached during the summer. The strength of the movement and the indication that it would continue well into 1950 prompted the executive committee of the Federal Open Market Committee to recommend to the full Committee that it authorize the executive committee to increase short-term rates somewhat in order to indicate a change from a policy of monetary ease to a policy of mild restrictions on the availability of bank reserves through open market operations. The purpose of this change in policy was to indicate the view on the part of monetary authorities that economic conditions had changed, that it was believed to be desirable to adopt a policy of some restraint and that, depending on developments, some further increases in rates might be called for. The full Committee approved the increase for the reasons that prompted the executive committee to make its recommendation.

#### 2. Authority to Effect Transactions in System Account.

The following direction to the executive committee, which was in the same form as the direction issued at the meeting on August 5, 1949, was approved.

The executive committee is directed, until otherwise directed by the Federal Open Market Committee, to arrange for such transactions for the