THIRTY-NINTH

ANNUAL REPORT

of the

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

COVERING OPERATIONS FOR THE YEAR

1952

desirable to make additional reserves available despite further large individual savings and accumulations of liquid funds and the use of these funds to meet current credit demands. Because of the potential inflationary situation, however, particularly the growing Federal cash deficit, the Committee felt that there should continue to be a minimum of direct purchases by the System and that the increased reserves needed by the market should be supplied mainly through member bank borrowings and use of repurchase agreements with dealers. The tighter money market was being reflected in a rising level of interest rates and suggested that, if credit demands should become excessive, an increase in the discount rate might be appropriate.

Under the circumstances, the Committee wished to be in a position to restrain excessive expansion in bank credit during the latter part of the year and at the same time to be free to moderate undue strain in the market. Thus, it was concluded that the general policy of limiting the availability of bank reserves that had been pursued by the System since October of 1951 was still appropriate and that that policy provided adequate flexibility for dealing with market influences in the absence of extremes of pressure in either direction. The above direction was therefore adopted in the same form and with the same limitations as the one adopted at the preceding meeting of the Committee, since it was felt that no change in existing objectives of credit policy was needed.

2. Amendment of Section 8 of Federal Open Market Regulation.

The Committee approved at this meeting an amendment to Section 8 of the Regulation of the Federal Open Market Committee with regard to the establishment of rates governing the purchase in the open market by Federal Reserve Banks of bankers' acceptances and bills of exchange of the kinds made eligible for purchase under the provisions of Regulation B of the Board of Governors of the Federal Reserve System. Prior to this action, the regulation had provided that the "rates of discount" in connection with such transactions should be established in accordance with the provisions of Section 14 (d) of the Federal Reserve Act, which meant that the rates were established by the Federal Reserve Banks subject to review and determination by the Board of Governors. Under the amendment adopted at this meeting, the reference to Section 14 (d) of the Federal Reserve Act was omitted. As a result, rates on transactions in bankers' acceptances and bills of exchange were brought more specifically under the direction of the Committee. The action contemplated that the Federal Open Market Committee from time to time would fix a minimum buying rate for bankers' acceptances and that the effective buying rates would be specified by the manager of the System open market account in the light of market conditions and developments and in accordance with any directives or limitations prescribed by the Federal Open Market Committee or the executive committee for the purpose of carrying out the policies of the Federal Open Market Committee.

Votes for this action: Messrs. Martin, Chairman, Sproul, Vice Chairman, Bryan, Earhart, Evans, Leach, Mills, Powell, Robertson, Szymczak, Vardaman, and Young. Votes against this action: none.

It was the view of the Committee that since any transactions in acceptances affect the availability of reserves for banks without the necessity of showing borrowings, they should be administered as open market operations and not as advances to member banks (except when they were made specifically as a rediscount for or an advance to a member bank and were treated by the bank as borrowing). Also, there had recently been some indication that the importance of the acceptance market might be increasing and, with the resumption of periods of seasonal tightness in the money market and some reduction in the liquidity position of banks, it seemed probable that the banks might find it advantageous to sell acceptances in order to obtain reserve funds. Thus, the Federal Reserve might be called upon to operate somewhat more actively in this market. This would be especially true if convertibility in the foreign exchanges were re-established and the way opened for the use of dollar acceptances to aid in financing world trade.

September 25, 1952

1. Authority to Effect Transactions in System Account.

The Committee adopted the following direction to the executive committee:

> 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 current and prospective economic conditions and the general credit situation of the country, with a view to exercising restraint upon inflationary developments, to maintaining orderly conditions in the Government security market, to relating the supply of funds in the market to the needs of commerce and business, and to the practical administration of the account; provided that the aggregate amount of securities held in the System account (including commitments for the purchase or sale of securities for 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 2 billion dollars.
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> The executive committee is further directed, until otherwise directed by the Federal Open Market Committee, to arrange for the purchase direct from the Treasury for the account of the Federal Reserve Bank

of New York (which Bank shall have discretion, in cases where it seems desirable, to issue participations to one or more Federal Reserve Banks) 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 at any one time by Federal Reserve Banks shall not exceed in the aggregate 2 billion dollars.

Votes for this action: Messrs. Martin, Chairman, Sproul, Vice Chairman, Bryan, Earhart, Evans, Leach, Robertson, Vardaman, and Young. Votes against this action: none.

The period between the meetings of the Federal Open Market Committee on June 19 and September 25, 1952 was marked by large Treasury financing operations in June, August, and September, a tight money market which became progressively tighter during the three months, a level of member bank borrowings at the Reserve Banks generally above a billion dollars, a rise in Federal Reserve holdings of securities, an increase in demand deposits and currency in circulation, and an upward tendency in short-term interest rates. The economy was operating at a high level, in a state of reasonable equilibrium.

Reserve System purchases of securities during this period were made principally at times of Treasury financing. The timing of such purchases, therefore, was not always what credit policy would have suggested. In ultimate effect, however, such purchases were partly offset by subsequent sales and over a period did not meet all the demand for reserve funds. System holdings at the time of this meeting were above those in late June, but the total was below that at the beginning of 1952. Some of the increased demand for reserves had been satisfied through borrowings by member banks which averaged around one billion dollars during most of this period, a level which caused banks to exercise a considerable degree of restraint in expanding the total volume of credit. While bank loans to business and those on real estate and consumer goods increased, there were declines in loans on securities and bank holdings of securities from the high points reached early in July at the time of the Treasury's issue of a 2⅜ per cent bond of 1958.

At this meeting, consideration was given to what the reasonable, noninflationary, credit demands during the remainder of the year might be, and it was felt that some increase in demand deposits and currency—the more active elements of the money supply—would be appropriate in an expanding economy. It appeared that such a growth would entail a substantial expansion during the remainder of the year, and demand for additional Federal Reserve credit might be a billion dollars or more. Since member bank borrowings already totaled a billion dollars and bank credit expansion seemed to be keeping within usual seasonal limits, it was felt that some of the additional reserves should be supplied through open market purchases in order to avoid undue restraint.

The Treasury had announced at the time of this meeting an issue of tax anticipation bills in the amount of 2½ billion dollars and it was expected that, with the growing Federal cash deficit, a further issue of about the same amount would be needed during the next few weeks.

The Committee considered that operations during the preceding three months had been reasonably successful in keeping an even flow of money through the economy without having had excessive reserve funds on the one hand, or undue contraction on the other, and that the policy of modest restraint with respect to the availability of reserves should be reaffirmed. The foregoing direction was therefore adopted, the first paragraph of which was in substance the same as that part of the direction issued at the preceding meeting.

The second paragraph of the direction was amended at this meeting to provide that purchases of special certificates of indebtedness direct from the Treasury for the temporary accommodation of the Treasury, under the authority of Section 14(b) of the Federal Reserve Act, should be made for the account of the Federal Reserve Bank of New York, with the understanding that that Bank, in its discretion, in cases where it seemed desirable, could issue participations to one or more Federal Reserve Banks. Previously, such certificates, which are carried on only a few occasions during the year and for only a few days at a time, had been held in the System account with resulting participation by all Federal Reserve Banks. The change was adopted for the purpose of simplifying the procedure for handling such transactions, particularly on days when some Reserve Banks were closed and others open, as on Saturday or on certain holidays. Since the amount of earnings from such special certificates is relatively small, the change in the practice would not affect significantly the earnings position of any Reserve Bank.

2. Repurchase Agreements.

At this meeting, the Federal Open Market Committee ratified an action taken by a canvass of the members of the Committee on July 22, 1952, with respect to the fixing of the rate on securities purchased under repurchase contracts, which, by the Committee's action of October 4, 1951, the Federal Reserve Banks were authorized to enter into with nonbank dealers in U. S. Government securities qualified to transact business with the System open market account. Such agreements could cover only short-term Treasury obligations and were required to be for periods of 15 days or less and for the purpose of aiding temporary money market adjustments. Before the action of July 22, such agreements had been made at rates close to the average issuing rate on the most recent issue of 3-month Treasury bills. The change ratified at this meeting provided that the rate on such agreements should be specified from time to time by the manager of the System open market account in the light of market conditions and developments and in accordance with any directives or limitations prescribed by the Federal Open Market Committee or the executive committee for the purpose of carrying out the current policies of the Federal Open Market Committee, but in no event should the effective rate be below whichever was the lower of (1) the discount rate of the purchasing Federal Reserve Bank on eligible commercial paper, or (2) the average issuing rate on the most recent issue of 3-month Treasury bills.

Votes for this action: Messrs. Martin, Chairman, Sproul, Vice Chairman, Bryan, Earhart, Evans, Leach, Robertson, Vardaman, and Young. Votes against this action: none.

The change in procedure for setting the rate was made principally because the issuing rate on Treasury bills had been higher than the discount rate during the past few weeks, and, under the previous condition, this situation would have required an increase in the rate on repurchase agreements. It was believed that this would not be an appropriate arrangement in certain types of credit situations such as that currently existing, particularly in view of the imminent Treasury refunding operation. It was therefore considered desirable to change the procedure so as to avoid the necessity of raising the repurchase rate above the discount rate whenever the issuing rate on Treasury bills moved higher than the discount rate.

December 8, 1952

1. 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 September 25, 1952, 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 current and prospective economic conditions and the general credit situation of the country, with a view to exercising restraint upon inflationary developments, to maintaining orderly conditions in the Government security market, to relating the supply of funds in the market to the needs of commerce and business, and to the practical administration of the account; provided that the aggregate amount of securities held in the System account (including commitments for the purchase or sale of securities for 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 2 billion dollars.

The executive committee is further directed, until otherwise directed by the Federal Open Market Committee, to arrange for the purchase direct from the Treasury for the account of the Federal Reserve Bank of New York (which Bank shall have discretion, in cases where it seems desirable, to issue participations to one or more Federal Reserve Banks) 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 at any one time by the Federal Reserve Banks shall not exceed in the aggregate 2 billion dollars.

Votes for this action: Messrs. Martin, Chairman, Sproul, Vice Chairman, Bryan, Earhart, Evans, Leach, Robertson, Vardaman, and Young. Votes against this action: none.

During the autumn months, economic activity and employment had advanced to higher levels than in the spring of 1952 but commodity prices had generally not advanced. Total credit demand had been at record peacetime levels reflecting in particular Federal deficit financing during the second half of 1952 and a more than seasonal increase in private credit demands. Reserve Bank credit other than "float" had risen about 1¼ billion dollars in the September-November period, considerably more than had been anticipated at the time of the September 25 meeting of the Committee. Only about a third of this increase had been supplied by Federal Reserve purchases of securities, and member bank borrowings had risen to over 1½ billion dollars.

The accelerated expansion of bank credit in excess of moderate seasonal demands during the autumn months was a matter of concern in view of the economy's intensive use of its physical resources and the large volume of credit already outstanding. At the same time, there was evidence that the peak of the defense program in terms of requirements for materials and manpower was close at hand and that the rise in public expenditures in the next six months would be much less than had been expected earlier. The economic outlook was by no means clear, however, and it appeared that credit and monetary policy would need to be kept alert to realignments in underlying forces that might affect long-term growth and stability so that such policies could be adjusted promptly and effectively to changing conditions as they developed.

It was the view of the Committee that the general outlook was for a high level of income and production over the next few months with no immediate evidence of price inflation. That view suggested that the Committee should remain on the alert but did not call for action to change the existing policy of modest restraint in furnishing any additional reserves, a policy which had been consistent with a stable price level and a high level of economic activity. Thus, the Committee renewed the direction set forth above in the same form as the direction issued to the executive committee at the meeting on September 25, 1952.