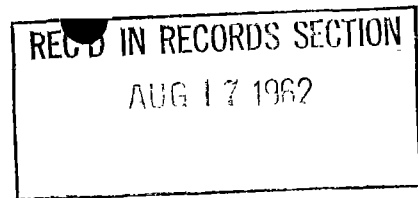




BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON



August 16, 1962.

CONFIDENTIAL (FR)

To: Federal Open Market Committee

From: Mr. Young

Question has been raised, as a matter of information, with regard to the procedure customarily followed when, in connection with a Treasury financing, securities held in the System Account portfolio are exchanged for the shortest term issue among two or more issues offered by the Treasury in exchange. The question was occasioned by a discussion of the terms of the current refinancing, and this memorandum is for the purpose of reviewing procedure and supplying the desired information.

It will be recalled that after the close of trading on Thursday, July 26, the Treasury announced that it would offer for cash subscription \$6.5 billion 3-1/2 per cent one-year certificates of indebtedness, \$1.5 billion 4 per cent bonds of February 1969, and up to \$750 million 4-1/4 per cent bonds of 1987-92. There were held in System Account \$3.7 billion 3-1/4 and 4 per cent notes maturing August 15. Subscription books were to be open only on Monday, July 30.

Upon studying the terms of the Treasury offer, the Account Manager concluded that it would be appropriate to subscribe for the shortest term issue (the 3-1/2 per cent certificates) to replace the notes in the Account portfolio maturing August 15. After discussing the matter by telephone with the Secretary

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of the Committee, he stated his intent during the morning telephone conference call on Friday, July 27, and reference was made to such intent in the memorandum on the conference call that was subsequently distributed to the members of the Committee. Then, in his supplementary report of open market operations dated July 31, which was distributed to the members of the Committee prior to the Open Market meeting on that date, the Account Manager stated: "On Monday, July 30, the System also subscribed for \$3.7 billion 3-1/2 per cent certificates to replace its holdings of 3-1/4 and 4 per cent notes maturing August 15."

At each meeting the Open Market Committee takes action to approve, ratify, and confirm the open market operations since the preceding meeting. Hence, the subscription for the 3-1/2 per cent certificates would be regarded as included among the operations approved, ratified, and confirmed by such action on the part of the Committee.

The foregoing procedure was in accord with usual practice on occasions of this kind and with the terms of the Committee's continuing authority directive, wherein the Federal Reserve Bank of New York is authorized and directed, to the extent necessary to carry out the current economic policy directive:

(a) To buy or sell United States Government securities in the open market, from or to Government securities dealers and foreign and international accounts maintained at the Federal Reserve Bank of New York, on a cash, regular, or deferred delivery basis, for the System Open Market Account at market prices and, for such Account, to exchange maturing United States Government securities with the Treasury or allow them to mature without replacement.....

On occasions when the Account Management has concluded that it would be advisable not to exchange maturing System holdings for the shortest term of several issues being offered by the Treasury, it has been the practice--when timing did not permit consideration of the matter at an Open Market meeting--for the Secretary to poll the members of the Committee on the Manager's

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recommendation. At the next subsequent meeting of the Committee, the action taken by the members of the Committee upon their being polled by the Secretary has been ratified.

The most recent such occasion was on February 5, 1962, when the members of the Committee, upon poll by the Secretary, approved the recommendation of the Manager that Account holdings of Treasury notes maturing February 15 and April 1, 1962, be exchanged in entirety through subscription for approximately \$3.3 billion 3-1/2 per cent certificates maturing February 15, 1963, and approximately \$1.5 billion 4 per cent notes maturing August 15, 1966. This action was ratified by the Committee at its meeting on February 13, 1962.

When he has concluded that it would be appropriate to exchange into the shortest term issue being offered, the Account Manager has either reported his intent at a meeting of the Open Market Committee or, as in connection with the current refinancing offer, reported his intent through the morning telephone conference call and the memorandum thereof subsequently distributed to the Committee members. The records do not appear to reflect an occasion on which the Secretary has polled the Committee, at the Manager's request, on a recommendation that Account holdings be exchanged into the shortest term issue being offered by the Treasury. However, such a procedure would seem appropriate should there be an instance when the Account Manager or those participating in the morning telephone call have any substantial question as to whether that course would be desirable. It would also be appropriate, of course, in any instance where a member of the Committee, upon learning of the Manager's intent through the memorandum on the daily telephone call, feels that there is reason for the Committee to be polled.


Ralph A. Young, Secretary,
Federal Open Market Committee.