

A meeting 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, May 3, 1949, at 10:30 a.m.

PRESENT: Mr. McCabe, Chairman
Mr. Sproul, Vice Chairman
Mr. Clayton
Mr. Draper
Mr. Earhart
Mr. Eccles
Mr. Gidney
Mr. Leach
Mr. McLarin
Mr. Szymczak
Mr. Vardaman

Mr. Morrill, Secretary
Mr. Carpenter, Assistant Secretary
Mr. Vest, General Counsel
Messrs. Thompson, Wheeler, and John H. Williams, Associate Economists
Mr. Rouse, Manager of the System Open Market Account
Mr. Thurston, Assistant to the Board of Governors
Mr. Riefler, Assistant to the Chairman, Board of Governors
Mr. Sherman, Assistant Secretary, Board of Governors
Mr. Ralph A. Young, Associate Director, Division of Research and Statistics, Board of Governors
Mr. Smith, Economist, Government Finance Section, Division of Research and Statistics, Board of Governors
Mr. Arthur Willis, Special Assistant, Securities Department, Federal Reserve Bank of New York

Messrs. Erickson, C. S. Young, Davis, and Peyton, alternate members of the Federal Open Market Committee

Messrs. Williams, Leedy, and Gilbert, Presidents of the Federal Reserve Banks of Philadelphia, Kansas City, and

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Dallas, respectively

Messrs. Demming, Assistant Vice President of the Federal Reserve Bank of St. Louis, and Raisty, Economist, Federal Reserve Bank of Atlanta

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meetings of the Federal Open Market Committee held on February 28 and March 1, 1949, were approved.

Upon motion duly made and seconded, and by unanimous vote, the actions of the executive committee of the Federal Open Market Committee as set forth in the minutes of the meetings of the executive committee held on February 28 and March 1, 1949, were approved, ratified, and confirmed.

A report of open market operations prepared by the Federal Reserve Bank of New York covering the period from March 1, 1949, to April 28, 1949, inclusive, was then read and discussed by Mr. Rouse. He also presented a supplementary report covering commitments executed on April 29 and May 2, 1949. Copies of both reports have been placed in the files of the Federal Open Market Committee.

Upon motion duly made and seconded, and by unanimous vote, the transactions in the System account for the period February 28, 1949, through May 2, 1949, inclusive, were approved, ratified, and confirmed.

Before this meeting, there had been brought to the attention of each member of the Committee a report of examination of the System open market account as of January 28, 1949, made in connection with the

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regular examination of the Federal Reserve Bank of New York and submitted by the examiner in charge for the Board of Governors. The report took no exception to the handling of the account and stated that the accounting procedures, records, and system of internal controls maintained and the degree of care exercised by the New York Bank in connection with the account continued to be regarded as satisfactory.

Upon motion duly made and seconded,
and by unanimous vote, the report was
received and ordered filed.

Before this meeting a memorandum of current economic conditions and the economic outlook for 1949, prepared by the staff of the Board's Division of Research and Statistics, was distributed to the members of the Committee. Mr. Ralph A. Young, Associate Director of the Board's Division of Research and Statistics, commented on the situation outlined in the memorandum stating that since the meeting of the Federal Open Market Committee on February 28, 1949, economic developments had shown a sufficiently broad and consistent downward movement to justify the expectation of continuing moderate recession as most likely for the remainder of this year, which would mean that inflation had been succeeded by a more or less extended period of decline. He added that to date the decline in employment, production, and prices from the high level reached last year had been relatively moderate and that the situation was one that was changing rapidly and would require continuing reviews of current tendencies. A copy of the memorandum has been

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placed in the files of the Federal Open Market Committee.

Mr. John H. Williams stated that he felt there was more of a fear of depression than an actual experiencing of one, that unemployment was astonishingly small and reductions in prices were disappointingly slow, that such declines in production as had taken place recently had been from extremely high levels, and that the decreases thus far could not be regarded as returning the economy to normal. He expressed the opinion that the real adjustment from the postwar inflation was ahead, but that he could not see anything to be alarmed about in the situation thus far. With respect to Federal Reserve policy, he stated that the System had not had a tight money policy, that any effort to ease money conditions to counter the recession would be starting from an already easy situation, and that he felt the System was likely to be frozen into a low-interest rate situation, about which it might not be able to do anything.

Mr. Thompson discussed increases that had taken place recently in productivity per manhour at industrial plants in the Fourth Federal Reserve District by means of weeding out less efficient employees, rearrangement and improvement in scheduling of production processes, and shutting down of some higher cost plants.

Mr. Raisty stated that some reductions in output had taken place in manufacturing plants in the Sixth Federal Reserve District but that the District as a whole had not been hurt materially by the decline to date.

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Mr. Riefler suggested there was danger in becoming too complacent about the decline, that when one considered the past ten years of rising prices and wages which set in motion the dynamics of inflation and the adjustments that would still have to take place, it would not be surprising if the index of industrial production should decline substantially further before the stage was set for a period of expansion.

Chairman McCabe reported briefly on developments since the last meeting of the Committee.

Reference was then made to a memorandum prepared by Messrs. Young, Smith, and Youngdahl of the Board staff with respect to Treasury cash requirements and bank reserves, and to two memoranda submitted by Messrs. Riefler and Rouse on the subjects (1) June refunding and possible new money borrowing, and (2) relative roles of marketable and full marketable issues in longer-range debt management and monetary operations. Copies of these memoranda had been handed to the members of the Committee before this meeting and copies have been placed in the files of the Committee.

Mr. Riefler stated that the last of the three memoranda above referred to was an interim report of the staff group appointed by the Committee to study and make a report on a program for conversion of long-term Treasury debt. He reviewed the experience with the various types of securities issued by the Treasury during and after the war and restated the suggestions contained in the memorandum with respect

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to future financing.

There followed a discussion of the interim report, the issues that might be used in future financing, and the problems presented by the present policy of supporting both the short- and long-term rates.

At the conclusion of the discussion, it was understood that the staff Committee would continue to work on the problem of a longer term refunding program so that when the time came to make a recommendation to the Treasury the Committee would be prepared to do so.

Preliminary to a discussion of recommendations to be made to the Treasury with respect to refunding of the June maturities, Mr. Rouse commented on the suggestions contained in the memorandum on June refunding and Chairman McCabe presented the recommendation of the executive committee on this subject as agreed upon at the separate meeting of that committee.

During the ensuing discussion it was agreed unanimously that, since a further increase in the short-term rate does not appear to be likely at this time, the Committee should adopt the suggestion of the executive committee and that, in their conversations with representatives of the Treasury, Messrs. McCabe and Sproul should recommend that the June 1 certificate maturity and the June 15 2 percent bond maturity be refunded into a new issue of Treasury notes due in 4 or 5 years to be priced at the market and offered at par.

It was recognized that if later there should be a further increase in the short-term rate the new issue might sell below par. However, it was suggested that such a change might not come soon enough to have such an

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effect but that in any event notes and certificates had sold below par before and there would be no real objection to the new issue going below par. The new issue would reduce the total of certificate maturities and would have a maturity date beyond the period in which the greater part of the 2 per cent bonds matured. It was expected that it would be made clear to the Treasury that the recommendation that the note be issued would not carry with it any commitment to support the issue at par or above except during the period immediately following its issue.

It was suggested, however, that it might be desirable for the July refunding also to be in the form of a 4 or 5 year note depending on what is done with the June maturities and subsequent market developments and that in the discussion which Messrs. McCabe and Sproul would have with representatives of the Treasury it might be desirable to recommend that at the same time the Treasury undertake to raise about \$1 billion of new money to meet its cash requirements. It was felt, however, that this suggestion should not be urged to the point of jeopardizing the proposed June refunding.

Turning to the question of subsequent refunding, it was agreed unanimously to authorize the executive committee, pending another meeting of the full Committee, to make such recommendations with respect to the July, September, and October financing as might appear to the executive committee to be desirable in the light of the action to be recommended to the Treasury in connection with the June maturities.

At this time Chairman McCabe withdrew from the meeting to keep another appointment.

Mr. Sproul then raised the question of the use of war loan balances and this subject was discussed in the light of the situation presented in the memorandum on Treasury cash requirements and bank

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reserves.

It was agreed unanimously that the scope of discretion in the use of war loan balances to affect the money market was greatly limited by the disappearance of the cash surplus of the Treasury and that the present program of consultation with the Treasury, which contemplated the use of available balances at least to neutralize the effect of Treasury operations in the money market, should be continued.

In a discussion of System bids for, and purchases and sales of, Treasury bills, Mr. Rouse stated that the objective had been generally to keep a neutral position and that, while for short periods recently it had been difficult to carry out that objective and rate policy simultaneously, he would suggest that it be continued fairly closely on a day to day basis with the idea, however, of putting no restraint on bank reserves, except in the event of a rate decline.

It was agreed unanimously that Mr. Rouse's suggestion should be carried out.

In a discussion of the authority to be given to the executive committee to direct transactions for the System open market account, Mr. Rouse suggested that, since another meeting of the Committee might not be held until late in August or early September, and in view of prospective market developments during that period, it would be desirable for the executive committee to have authority to increase and decrease the account by as much as \$3 billion.

Thereupon, upon motion duly made and seconded, the following direction to the executive committee was approved unanimously, with the understanding that the

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limitations contained in the direction would include commitments for the System open market account:

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 stable and 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 \$3,000,000,000.

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 \$1,500,000,000.

It was tentatively agreed that the next meeting of the Federal Open Market Committee would be held during the week beginning August 29, 1949.

Thereupon, the meeting adjourned.

Chester Morrie
Secretary.

Approved:

Thomas B. U. Case
Chairman.