A meeting of the executive committee of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System in Washington on Saturday, March 1, 1947, at 11:05 a.m.

PRESENT: Mr. Eccles, Chairman
Mr. Sproul, Vice Chairman
Mr. Draper
Mr. Vardaman
Mr. Davis

Mr. Morrill, Secretary
Mr. Carpenter, Assistant Secretary
Mr. Vest, General Counsel
Mr. Thomas, Economist
Mr. Rouse, Manager of the System Open Market Account
Mr. Sherman, Assistant Secretary to the Board of Governors
Mr. Musgrave, Chief, and Mr. Smith, Economist, of the Government Finance Section of the Division of Research and Statistics of the Board of Governors

Mr. Clayton, member of the Federal Open Market Committee
Messrs. John H. Williams and Stead, Associate Economists of the Federal Open Market Committee

Upon motion duly made and seconded, and by unanimous vote, Mr. Sproul was reelected Vice Chairman of the executive committee to serve until the election of his successor at the first meeting of the executive committee after February 29, 1948.

In connection with the authority to be given to the Federal Reserve Bank of New York to execute transactions for the System account Chairman Eccles suggested that for substantially the same reasons as prompted the reduction in the limitation contained in the first paragraph of the direction issued by the full Committee to the executive committee, the limitation contained in the first paragraph of the existing direction to the Federal Reserve Bank of New York be reduced from $750 million to $500 million. The suggestion was also made that the limitation of $750 million in the second paragraph of the direction be increased to $1.5 billion to take care of possible Treasury needs during the period before the next meeting of the committee, but it was felt that there would be ample time to increase the limitation if that should be found necessary.

Thereupon, upon motion duly made and seconded, and by unanimous vote, the executive committee directed the Federal Reserve Bank of New York, until otherwise directed by the executive committee,

(1) To make such purchases, sales, or exchanges (including replacement of maturing securities and allowing maturities to run off without replacement) for the System account, either in the open market or directly from, to, or with the Treasury, 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 7/8 per cent for one-year certificates and 2-1/2 per cent for 27-year bonds restricted as to ownership; provided (a) that the total amount of securities in the account at the close of this date shall not be increased or decreased by more than $500,000,000 [exclusive of bills purchased outright in the market on a discount basis at the rate of 3/8 per cent per annum and bills redeemed at maturity, and special short-term certificates of indebtedness purchased for the temporary accommodation of the Treasury pursuant to paragraph (2) of this direction], and (b) that this paragraph shall not limit the amount of Treasury bills purchased pursuant to the direction of the Federal Open Market Committee issued under date of March 1, 1945, or the redemption of such bills;

(2) To purchase direct from the Treasury for the System open market account 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 $750,000,000; and

(3) Upon approval by a majority of the members of the executive committee, which may be obtained by telephone, telegraph, or mail, to make such other purchases, sales or exchanges for the account as may be found to be desirable within the limits of the authority granted to the executive committee by the Federal Open Market Committee.

In taking this action, it was understood that the limitations contained in the direction included commitments for purchases or sales of securities for the System account.

Chairman Eccles referred to the memorandum presented at the meeting of the Federal Open Market Committee on February 28, 1947, relating to the issuance of a long-term security by the Treasury. He stated that the draft of the memorandum had been approved as to substance, with the understanding that the final form would be determined by the executive committee before the memorandum was sent to the Treasury. He suggested that all members of the executive committee study the memorandum carefully and submit any suggested language changes that they might have to propose.

Upon motion duly made and seconded, it was agreed unanimously that the memorandum should be sent to the Treasury, with such changes in wording as the Chairman and Vice Chairman of the committee agreed upon.

Secretary's note: The memorandum sent to the Treasury in accordance with this arrangement was as follows:

"ISSUANCE BY THE TREASURY OF A NEW LONG-TERM SECURITY

"Proposals for the issuance of additional long-term securities, as part of the Treasury's refunding program, have been under discussion for the past year. Since replacement of maturing issues with long rather than short-term maturities will result in a higher cost of carrying the debt, any such program must be tested against broad objectives of credit and debt management policy.

"<u>Some Long-term Refunding Desirable</u>

"On this basis, some additional supply of long-term Government securities would be desirable when:

(1) new institutional and savings funds become available which are not being placed in private investment outlets:

(2) the increasing volume of such funds and the static supply of long-term maturities threatens to depress the issuing rate on long-term Government bonds below 2-1/2 per cent. (A decline in long-term rates from this cause must be distinguished from a decline due to debt monetization by commercial banks.)

(3) the funds raised by the issuance of additional long-term securities can be applied to the redemption of maturing obligations which are held by the banking system. The retirement of securities held by commercial banks would help to reduce demand deposits, while retirement of securities held by the Federal Reserve banks would assist in keeping member bank reserves under some pressure. This would contribute to preventing renewed inflationary credit expansion. Reliance on refunding operations for the transfer of bank-held bonds to nonbank investors is increasingly important at this time in view of the prospect for tax reduction and, in consequence, of reduction in budget surplus available for debt retirement.

"At the recent meeting with Treasury officials, the representatives of insurance companies appeared to justify the issuance of long-term bonds by the Treasury, both from the standpoint of the amount of institutional funds currently available for investment, and from the standpoint of the stabilizing effect of such an issue upon investment yields in general. Even though their presentation may not have fully met the requirements of conditions (1) and (2) above, it does give support to condition (3). The Committee considers it desirable, therefore, to make a beginning in the direction of a long-term refunding program. In the future, this program may be adapted to new situations as they develop.

"<u>Marketable Issue Not Called For</u>

"While these considerati ns justify the issuance of some long-term securities, our objective would not be served by an offering of marketable securities.

(1) A marketable security would provide renewed opportunity for investment institutions to 'play the pattern of interest rates'. At a coupon rate of 2-1/2 per cent, a market obligation would attain an immediate premium and a supplementary premium would develop as the issue moved toward maturity. In this way, holders of such an issue would be able to obtain a return considerably above 2-1/2 per cent by selling at a premium some time during the life of the obligation. Past experience indicates that this would be done by many purchasers of the new issue.

(2) Unless the new issue was quite small, it would be accompanied by substantial sales to commercial banks of securities (due or callable in more than one year), now held by institutional investors. Banks would sell short securities to the Reserve System. The 'rollover' would be completed as institutional investors replaced holdings which they had sold by subscribing to the new issue. The result would be increased rather than reduced monetization of debt.

(3) With a stabilized level of interest rates on long-term Government securities, such issues are, in effect, demand obligations of the Federal Reserve System. If a market obligation is issued, the Treasury would pay long-term rates on bonds which the System would make it possible for investors to buy on a short-term basis.

"For these and the following reasons, the Committee strongly advises against the issuance of a marketable long-term security at this time.

"<u>Non-marketable Issue Serves the Purpose</u>

"A non-marketable Treasury issue of the Series G type would be much superior in meeting the objectives of credit and debt management policy.

"(1) If there are bona-fide investment funds seeking a safe and long-term placement, a bond of the G type should be as satisfactory as a marketable security.

(2) A market bond would require a fixed offering and a complicated system of allotment, the amount and timing of which would be difficult to gauge. A bond of the G type could be placed on sale for an undetermined period and an indefinite amount. Since these

"bonds would be registered, subscription, if necessary, could be limited to a percentage of new money accrued within a stated period.

(3) The G type issue would attract mostly bona-fide investors and minimize the 'rollover' problem.

(4) The issuance of a G type bond would tend to stabilize all long-term interest rates.

(5) In view of the present uncertain economic outlook, the Treasury needs to retain flexible control over the issuance of long-term securities to nonbank investors.

(6) Investors would receive a long-term rate of interest for long-term holdings only.

"The apparent lack of interest in a restricted issue, on the part of institutional investors, may well reflect their hope of obtaining better terms. After it is evident that better terms will not become available in the near future, a non-marketable issue of the G type might be expected to find a satisfactory institutional demand. If not, this would be in itself an indication that there is no real surplus of funds for investment in long-term Government securities in excess of current opportunities for buying private issues. The availability of a restricted tap issue of Series G type bonds, at this time, would offer an adequate protection for maintaining the long-term rate at 2-1/2 per cent and the Committee recommends that such an issue be made available."

Thereupon the meeting adjourned.

Chester Morrill
Secretary.

Approved: M S Eccles
Chairman.