

TWENTY-NINTH
ANNUAL REPORT

of the

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM



COVERING OPERATIONS FOR
THE YEAR

1942

1. Purchases by Federal Reserve Banks of Treasury Bills at Fixed Discount Rate.

On April 30, 1942, in connection with the announcement of the May Treasury financing, which included an increase to \$250,000,000 in the weekly offering of Treasury bills, all the members of the Federal Open Market Committee agreed upon a direction which was immediately issued to the twelve Federal Reserve Banks to purchase for the System open market account all United States Treasury bills that might be offered to such Banks on a discount basis at a rate of $\frac{3}{8}$ per cent per annum.

At this meeting, upon motion duly made and seconded, it was voted unanimously to approve, ratify, and confirm the direction and to continue it in effect until otherwise directed by the Federal Open Market Committee.

After the meeting of the Federal Open Market Committee, which was held on March 2, 1942, members of the Committee continued to confer from time to time with representatives of the Treasury on the subject of the formulation of a Treasury financing program which would be designed to attract as many funds as possible from sources other than commercial banks and regarding the methods by which the Federal Reserve System would supply such reserves as were necessary to assure the successful financing of the war. In connection with the latter problem and in order to carry out the existing open market policy, the members of the executive committee of the Open Market Committee had agreed that the general market should be maintained on about the then existing curve of rates (but that this did not mean special support for issues which might be out of line or that any issue must be held at par or at any other fixed price), and that the Federal Open Market Committee should use its best judgment with respect to the market and with regard for the relation of the market to the general financing program. The direction to the Federal Reserve Banks to purchase Treasury bills on a fixed discount basis was agreed upon by the members of the Committee as a means of stabilizing the bill market, of effecting a broader distribution of bills, and of encouraging banks and others to utilize available liquid funds for the purchase of bills with the assurance that, if at any time it was necessary to sell bills to adjust their individual positions, the Federal Reserve Banks of their respective districts would purchase the bills at the announced rate.

2. Authority to Effect Transactions in System Account.

Upon motion duly made and seconded, the following direction to the executive committee was approved by unanimous vote:

"That the executive committee be 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 for the purpose of maintaining about the present general level of prices and yields of Government securities or for the purpose of maintaining an adequate supply of funds in the market; provided that the aggregate amount of securities held in the account at the close of this date (other than Treasury bills purchased

pursuant to the direction of the Federal Open Market Committee issued under date of April 30, 1942) shall not be increased or decreased by more than \$500,000,000."

The foregoing direction differed from the one approved at the previous meeting of the Committee in that it provided for purchases either in the open market or directly from the Treasury and for purchases either for the purpose of maintaining the general level of prices and yields of Government securities or for the purpose of maintaining an adequate supply of funds in the market, and made it clear that Treasury bills purchased by Federal Reserve Banks pursuant to the direction issued April 30, 1942, were not restricted by the limit placed upon the authority of the executive committee by this direction.

Open market operations in the previous months had been largely for the purpose of maintaining about the existing level of rates of Government securities in a period when the Treasury was offering a large volume of new securities, and for the purpose of furnishing funds to banks whose reserves were being reduced through the purchase of additional amounts of Government obligations. There was agreement that operations in the open market during the period before another meeting of the Committee would continue to be largely for these purposes and that the terms of the direction to the executive committee should be changed to relate the authority of the executive committee specifically to these conditions.

On March 27, 1942, the Second War Powers Act was approved, which authorized the Federal Reserve Banks, until December 31, 1944, or such earlier time as Congress or the President may designate, to purchase Government securities directly from the Treasury, provided that the aggregate amount of such securities purchased and held at any one time does not exceed \$5,000,000,000. In accordance with this change in the law, the authority of the executive committee was expanded to permit direct purchases of securities from the Treasury in order to provide for temporary accommodations to the Treasury during periods of Treasury financing or other periods when it was desirable for a brief time to allow Treasury balances at the Reserve Banks to decline.

MEETING ON JUNE 22, 1942

Members present: Mr. Eccles, Chairman; Mr. Sproul, Vice Chairman; Mr. Szymczak, Mr. McKee, Mr. Ransom, Mr. Draper, Mr. Evans, Mr. Williams, Mr. Gilbert, Mr. Young, Mr. Leedy.

1. Authority to Effect Transactions in System Account.

Upon motion duly made and seconded, the following direction to the executive committee was approved by unanimous vote:

"That the executive committee be 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 practical administration of the account, or for the purpose of maintaining about the present general level of prices and yields of Government securities, or for the purpose of maintaining an adequate supply of funds in the market, or

for the purpose of granting temporary accommodation to the Treasury; provided that the aggregate amount of securities held in the account at the close of this date (other than Treasury bills purchased pursuant to the direction of the Federal Open Market Committee issued under date of April 30, 1942) shall not be increased or decreased by more than \$500,000,000."

At this meeting the Federal Open Market Committee reviewed the important problems relating to the Treasury financing and Federal Reserve System monetary policies which had been considered by members of the Committee in discussions with representatives of the Treasury since the meeting of the Committee on May 8. The members of the Committee were unanimously of the opinion that during this period of further development by the Treasury of a program of war financing the directions to the executive committee should be in such form as would cover the continuance of the existing policy of arranging for such open market operations as may be necessary for the practical administration of the System account, to maintain the market for outstanding issues of Government securities at about the existing price level, to supply needed funds to the market in connection with Treasury financing operations, and to grant temporary accommodations to the Treasury.

MEETING ON AUGUST 3, 1942

Members present: Mr. Eccles, Chairman; Mr. Szymczak, Mr. McKee, Mr. Ransom, Mr. Draper, Mr. Evans, Mr. Williams, Mr. Gilbert, Mr. Young, Mr. Leedy.

1. Authority to Increase the Amount of Securities in System Account.

On July 6, 1942, at the request of the members of the executive committee, all the members of the Federal Open Market Committee approved an increase from \$500,000,000 to \$850,000,000 in the limitation on the authority of the executive committee to increase or decrease the amount of securities held in the System open market account.

At this meeting of the full Committee, upon motion duly made and seconded, and by unanimous vote, this action of the members of the Committee was approved, ratified, and confirmed.

Early in July it appeared that the amount of securities that would have to be purchased for the System account in order to continue the policy agreed upon at the previous meeting of the Federal Open Market Committee would exceed the limit which had been placed on the authority granted to the executive committee to increase the amount of securities held in the account. Accordingly, the members of the executive committee asked the remaining members of the full Committee to agree to an increase in the limitation on the authority of the executive committee and this request was approved unanimously. Between the meeting on June 22, 1942, and this meeting, the security holdings of the Federal Reserve Banks were increased by \$611,000,000 to \$3,159,963,000.

2. Purchase by Federal Reserve Banks of Treasury Bills under a Repurchase Option.

Upon motion duly made and seconded, the following supplementary direction to the Federal Reserve Banks was approved by unanimous vote:

"Supplementing the direction of April 30, 1942, issued by the Federal Open Market Committee to the Federal Reserve Banks to purchase all Treasury bills that may be offered to such Banks on a discount basis at the rate of $\frac{3}{8}$ per cent per annum, any such purchases shall, if desired by the seller, be upon the condition that the Federal Reserve Bank, upon the request of the seller before the maturity of the bills, will sell to him Treasury bills of like amount and maturity at the same rate of discount."

This action had the effect of amending the direction as then in effect to give to the seller of bills to a Federal Reserve Bank, when desired, the right of repurchase. Treasury bills in the hands of banks thus became practically equivalent to excess reserves. In the event it became necessary for a bank or other holder of bills temporarily to adjust his cash position, he could sell the bills to a Federal Reserve Bank under the repurchase option and reacquire them after the need for funds had passed, thus avoiding the necessity of selling the bills in the market to meet a temporary situation. It was believed that this arrangement would encourage fuller investment of idle short-term funds and thereby bring about a wider distribution of bills.

3. Authority to Effect Transactions in System Account.

Upon motion duly made and seconded, the following direction to the executive committee was also approved by unanimous vote:

"That the executive committee be 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 practical administration of the account, or for the purpose of maintaining about the present general level of prices and yields of Government securities, or for the purpose of maintaining an adequate supply of funds in the market, or for the purpose of granting temporary accommodation to the Treasury; provided that the aggregate amount of securities held in the account at the close of this date (other than Treasury bills purchased pursuant to the directions of the Federal Open Market Committee issued under dates of April 30 and August 3, 1942) shall not be increased or decreased by more than \$1,000,000,000."

This direction, which was in the same form as the direction to the executive committee approved at the meeting of the Federal Open Market Committee on June 22, 1942, except that the limitation on the direction was increased from \$500,000,000 to \$1,000,000,000, was adopted for substantially the same reasons as had attended the approval of the earlier direction. The increase in the limitation on the authority, which was approved in the light of further discussions with Treasury representatives of Government financing and Federal Reserve System policies, was based on the expectation that with the rapid growth of the Treasury's needs for funds to finance the war program substantial additional amounts of securities would have to be purchased to effectuate the policies adopted by the Committee, and, therefore, the members were in agreement that the executive committee, in carrying out the direction, should be in a position to meet any situation that could be foreseen over the next few weeks.