

Thus, while Federal Reserve purchases would tend, other things being equal, to depress interest rates on FHL Bank obligations, Federal Reserve sales (or foregone purchases) would at the same time put upward pressure on yields of short-term Treasury issues. At best, a Federal Reserve buying program of this type would simply help to keep spreads between yields on short-term Treasury and FHL Bank issues from widening as much as they usually would in the assumed circumstances of generally rising short-term rates and expanding FHL Bank offerings.

In short, Federal Reserve buying of FHL Bank debt--even if undertaken directly, as well as in the open market--would probably not be very effective in insulating the Home Loan Bank System from high interest costs at times of severe credit squeeze. Since large-scale buying of FHL Bank debt would also present problems of market domination, as already noted, and create important technical difficulties for day-to-day management of the Federal Reserve open market portfolio, it is not at all clear that such a policy would on balance produce a net social benefit.

The Board of Governors does, of course, recognize that occasions may arise when FHL Banks should be provided with otherwise unavailable funds for lending to S and L's faced with a severe liquidity crisis. Emergency arrangements were made during the 1966 credit squeeze for Federal Reserve Banks to serve as lenders of last resort in such situations through their discount operation. Similar arrangements would again be made should similar circumstances develop in the future. But in the last analysis continued efforts to produce fundamental institutional reforms are likely to be most effective in ameliorating the severity of pressures on mortgage and housing markets during periods of tight money. Since 1966, both Government and industry groups have been actively studying and promoting a number of such proposals for institutional reform. I believe these efforts should continue to be actively encouraged.

I hope that these comments will be helpful to you in responding to Commissioner Martin.

Sincerely yours,

*(Signature)*

Wm. McC. Martin, Jr.

(Whereupon, at 12:15 p.m., the committee adjourned.)