

by feeding that kind of rate situation, may turn out to aggravate the problems of the mortgage market in particular more than if they spaced out their financing over a period of time. This is particularly true with Treasury bonds in good part appealing to a somewhat different set of lenders than the lenders that are particularly heavy in the mortgage market.

I would also make one other point in this connection. I do not think the Treasury has any intention of going out and issuing a tremendous amount of long-term bonds without regard to its effect on the sectors of the economy that may already in some sense be under more relative pressure than other areas.

Representative REUSS. The less tremendous the amounts, the less the impact on these problems. What are they?

Mr. VOLCKER. I think there are, essentially, two problems here, Mr. Reuss. I will take them up in the reverse order that I mentioned in my statement.

The one is that the heavy schedule of Treasury borrowing operations, and perhaps most particularly the very large Treasury refunding operations that have been necessary in recent years to keep this short-term debt rolled over, means that the Treasury is in the market quite frequently, at least each quarter and sometimes oftener. If, during this period, the Federal Reserve finds that they need to take some action, it is circumscribed to some extent in terms of not being able to take action that might upset the whole structure of credit markets during the period of a Treasury offering of billions of dollars worth of securities, when those securities are hanging out, so to speak, in the market waiting for buyers.

Representative REUSS. I had thought that the Fed had emancipated itself from the Treasury in the historic and highly publicized accord of 1951. It turns out they are still chained to the old workbench?

Mr. VOLCKER. I think they have emancipated themselves, if that is the right word, from any direct support of Treasury financing, and I think that is entirely appropriate. They cannot emancipate themselves from the responsibility for maintaining viable money and credit markets in general. There is always a problem during these offerings. The very mass of Treasury operations in the market is such that you could get adverse repercussions not only with respect to the success of that particular Treasury financing but spreading out and rippling through the credit market as a whole. You would create in the end the kind of disorderly conditions in the markets—the kind of discontinuity in markets—that would affect the prospects for all kinds of borrowers, including specifically State and local government borrowers and mortgage borrowers, if Treasury financing is not handled in a reasonably orderly manner.

Also they do, as part of their own responsibility, quite properly I think, feel some responsibility for maintaining not easy conditions but more or less steady conditions—on an “even keel”—during the period that the Treasury is in the market. I think what you find, in an attempt to do this, is that during a time of very heavy credit demand in all sectors of the economy, an even keel may provide something of an open door for that period to any borrower who comes into the market because his need, in effect, must be accommodated along with the Treasury's, or the purpose of the even-keel operation is defeated. I think you saw some elements of this kind of a situation perhaps more particularly