

The meeting of the Federal Open Market Committee was reconvened in the offices of the Board of Governors of the Federal Reserve System in Washington on April 4, 1937, at 11:15 a.m.

PRESENT: Mr. Eccles, Chairman
Mr. Harrison, Vice Chairman
Mr. Broderick
Mr. Szymczak
Mr. McKee
Mr. Ransom
Mr. Davis
Mr. Sinclair
Mr. McKinney
Mr. Martin
Mr. Peyton (alternate for Mr. Day)

Mr. Morrill, Secretary
Mr. Goldenweiser, Economist
Mr. Williams, Associate Economist
Mr. Wyatt, General Counsel
Mr. Dreibelbis, Assistant General Counsel
Mr. Burgess, Manager of the System Open Market Account
Mr. Carpenter, Assistant Secretary of the Board of Governors
Mr. Thurston, Special Assistant to the Chairman of the Board of Governors

Chairman Eccles stated that an informal meeting of the members of the executive committee of the Federal Open Market Committee was held with the Secretary of the Treasury and members of his staff at Mr. Morgenthau's home last night, where the problem under consideration was fully discussed, after which Secretary Morgenthau stated he would be willing to hold in abeyance any action by the Treasury Department, if it could be understood that the Federal Reserve System would take action through open market operations looking toward effectively preventing the recurrence of a disorderly market and that,

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if System action were not satisfactory, the Treasury Department would then take such action as it saw fit. It was made clear, Chairman Eccles said, that the Secretary did not think that the market could or should be "pegged" but that he felt that the precipitous decline in the market, which in his opinion was brought about by the increase in reserve requirements of member banks, should be corrected by action which would restore the market to an orderly condition.

Chairman Eccles expressed the feeling that the System should increase excess reserves of member banks by as much as \$250,000,000 if necessary over the period of adjustment to the May first increase in reserve requirements and said that if the Committee was not willing to adopt that policy he would favor a cancellation of the May first increase in reserve requirements.

Mr. Harrison said that in the light of Chairman Eccles' position it was important that before any action was taken by the Federal Open Market Committee it be advised what the Board proposed to do with respect to the cancellation of the May first increase in reserve requirements. A canvass of the members of the Board indicated that there were not four members in favor at that time of voting to rescind the May first increase.

In connection with a consideration of the relative merits of open market operations by the Federal Reserve System and a program of desterilization of gold by the Treasury, Chairman Eccles expressed the opinion that the problem was one of easing over the temporary period of adjustment to the increased reserve requirements for member

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banks, that it should be met as a problem of credit management and that the Federal Reserve System should take such action as would preserve for the System its leadership in this field.

The suggestion was made that each member of the Committee should express himself on the question whether some action should be taken and, if in his opinion action was necessary, whether it should be by way of cancellation of the May first increase in reserve requirements, open market operations, or desterilization of gold.

Mr. Martin said he had come to the conclusion that some action should be taken, that it should be by way of authorization to the executive committee to engage in open market operations according to its judgment from day to day in the light of market developments, in order to prevent disorderly conditions, and that the May first increase in reserve requirements should not be canceled.

Mr. Harrison said he saw no reason for any action at this time other than to continue the policy of making shifts in maturities and that he did not feel there was anything in the situation at the present time which would justify the Federal Reserve System in taking action to increase excess reserves. He referred to the inflationary tendencies which were developing in certain fields and expressed the opinion that any action taken to stabilize the bond market which would increase excess reserves would be interpreted as encouraging the inflationary movement. He also felt that the Government securities markets had not yet reached the point where the System would be

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justified in taking the risks which would attend an increase in excess reserves and that he would not be willing today to approve an increase in the System's portfolio during the coming week regardless of the condition of the market, but that he would be agreeable to granting the executive committee authority to act in the light of market conditions as they develop, to prevent a disorderly market, without the requirement of the existence of an "emergency" but with definite limitations under which the executive committee would operate. He also said that it appeared that the committee was faced with a situation in which the Treasury had taken the position that, if effective action were not taken by the Federal Reserve System by way of increasing its portfolio, the Treasury would take separate action, that Secretary Morgenthau had made it clear at the conference last evening that, while he was requesting that action be taken by the System, if a public statement were issued and the market did not continue to decline during the coming week it would not be expected that the System would take action to increase the System account beyond a very nominal amount. The Secretary had also made it clear, Mr. Harrison said, that if he were not satisfied with the results of any action taken by the System action would be taken by the Treasury, and, in this situation, he (Mr. Harrison) questioned whether it would not be preferable for the Treasury to take independent action rather than to have the System take action solely for the purpose of avoiding Treasury action.

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Mr. Sinclair was opposed to any increase in the System account which would not have a relation to preventing disorderly conditions in the market, but said he would favor placing authority, within limitations but without using the word "emergency", in the executive committee to take such action as might be desirable in an endeavor to keep the market from becoming disorderly. He felt that a substantial increase in the portfolio without regard to the condition of the market would further unsettle the market and might result in additional selling. He concluded with the statement that he would not favor a cancellation of the May first increase in reserve requirements and that, in view of all the circumstances, he felt it would be more desirable to grant authority to the executive committee, with certain limitations, than for the Treasury to take independent action through sterilization of gold.

Mr. Harrison said he would definitely prefer action through open market operations to a cancellation of reserve requirements if they were the only two alternatives and that while he did not favor directing the executive committee to increase the portfolio regardless of the condition of the market he would favor granting discretionary authority to the executive committee to take such action within limitations which would be defined with the general purpose of avoiding a disorderly market. He felt that if authority were given to the executive committee to increase the portfolio the resolution approved at the last meeting of the Federal Open Market

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Committee with respect to shifts of securities in the System account should be changed to increase to \$1,000,000,000 the amount of securities with maturities within two years that must be maintained in the account.

The meeting recessed at 1:30 p.m. and reconvened at 2:25 p.m. with the same attendance as at the morning session.

Mr. McKinney said that he concurred in the feeling that a cancellation of the May first increase in reserve requirements would be a mistake, that he felt the System should cooperate in meeting the existing problem, and that he would favor granting such authority to the executive committee as would enable it, in the exercise of its judgment, to demonstrate that the System intends to take definite action toward preventing a disorderly market.

In engaging in open market operations, Mr. McKinney said, the System would inject into the market only such amounts of funds as the executive committee, in the exercise of its discretion, might find necessary to attain the desired objective, whereas, the cancellation of the May 1st increase in reserve requirements would be an arbitrary action and would not bear any direct relationship to the amount of funds required. Moreover, he said, by undertaking open market operations (including both purchases and sales of securities) an excellent opportunity would be presented to overcome the rigidity of the System's portfolio which had existed since November, 1933, and concerning which there had been much discussion during the last two or three years.

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Mr. Peyton said he would favor giving the executive committee authority to act, within limitations to be determined, to prevent a disorderly market and with due regard to encouraging investors to come into the market so that the Government security holdings of member banks may be placed in the hands of private investors. He expressed disapproval of the issuance of any public statement at this time because of his feeling that it would have an effect opposite to that which was desired. He added that, if the results of open market operations carried out under the authority granted to the executive committee were not satisfactory to the Treasury, he would not object to the Treasury desterilizing gold provided the System and the Treasury were in agreement and that agreement were made known to the public. He did not feel that a cancellation of the May first increase in reserve requirements would be effective in the present situation.

Mr. Ransom said that he would prefer that action be taken by the Treasury, in cooperation with the Board, to desterilize gold, that, if the Treasury would not take this course, his second choice would be open market operations within certain limitations, and that he would not favor cancellation of the May first increase in reserve requirements.

Mr. Davis said that he favored action and that his first choice would be to cancel the May 1 increase in reserve requirements; second, to engage in open market purchases; and only as a last resort, Treasury

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action to desterilize gold. He pointed out that the total increase in excess reserves resulting from the combined proposed action of the Treasury in desterilizing gold and the Reserve System through open market purchases, if carried out fully, would amount to \$650,000,000, or almost as much as the May 1 increase in reserve requirements, and expressed the opinion that cancellation of the final increase was the most direct method of reaching the end sought.

Mr. Broderick said that he would not favor action at this time, that he would be opposed to cancellation of the May first increase in reserve requirements, but that he would vote reluctantly for a resolution authorizing the executive committee to increase the System portfolio under specific limitations as to its authority and with the understanding that the committee would be expected to discontinue such operations should it appear that the action was having an effect contrary to that desired. He felt that in the long run a natural adjustment in the market would be best for the country.

Mr. Szymczak said that he would prefer to take no action at this time and to await further developments but that, if the increase in reserve requirements were thought by a majority of those present to be the cause of the present condition, he would favor rescinding the May first increase in reserve requirements. He said that he would be willing as a second choice to authorize the executive committee to act to such extent as market conditions require.

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Mr. McKee stated that he felt that some action was necessary in order to correct the attitude of mind now existing towards the Government bond market; that, while the cancellation of the May first increase in reserve requirements would be his first choice of action, such a course seemed impossible of accomplishment in view of the probable lack of a majority of the members of the Board of Governors favoring such action; and that, therefore, he would next favor action in the form of open market operations. He further stated that, regardless of which action was taken, either by the Federal Open Market Committee or the Board of Governors, he favored an immediate announcement to the press of the action decided upon in order that the entire country might be advised simultaneously.

At this point a question was raised as to whether the action of the Board in increasing reserve requirements was the major cause of the unsettled condition in the market and all of the members, with the exception of Messrs. McKee and Davis, stated that they did not think it was the major cause and that the recession in the Government securities market probably would have taken place regardless of the increase in reserve requirements. Mr. McKee felt it was the major cause and Mr. Davis felt that if not the major cause, it was the immediate cause.

Chairman Eccles stated that if the Treasury did not sterilize gold it would be under the necessity of borrowing approximately \$300,000,000 of additional funds between now and June, that, as the

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recent increase in Treasury bill rates was brought about largely by the tightened credit situation resulting to some extent from the action of the Board in increasing reserve requirements, he felt the System should take action to prevent a further increase in the bill rate and that, in order to accomplish this result and in view of the fact that, contrary to the usual situation, the System account, because of shifts from bills to bonds during the recent period, held practically no bills which will mature on Monday, April 5, he would increase the System portfolio on Monday by the purchase of \$5,000,000 or \$10,000,000 of existing bills.

Mr. Harrison read a draft of a resolution prepared by him which would authorize the executive committee to buy or sell up to \$250,000,000 of Government securities if in its judgment conditions in the money market over the period of adjustment in the reserve position of member banks make such purchases desirable as a means of using the System's influence toward avoiding drastic or sudden movements of money rates either short or long term.

There followed a discussion of the question whether the authority to be granted to the executive committee should be regarded as a mandate to buy Government securities regardless of conditions in the Government securities market or as a discretionary authority to be exercised by the executive committee in the light of conditions as they develop.

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Chairman Eccles submitted a draft of a resolution with the statement that if it were approved and even if the market were steady tomorrow the executive committee, acting under the authority of the resolution, would be required to buy some bills and that the present policy of shifts would be coordinated with such purchases under an authority to be granted to the executive committee to make shifts to an extent which would not reduce below \$1,000,000,000 the securities in the account with maturities within two years.

The resolution submitted by Chairman Eccles was considered and changed to cover sales as well as purchases of securities with a view to preserving an orderly market. As amended, the resolution read as follows:

"The Federal Open Market Committee directs the executive committee to make such purchases or sales of United States Government securities, beginning April 5, 1937, as may be necessary with a view to preserving an orderly market, but to make purchases of not less than \$25,000,000 during the week beginning April 5, 1937, provided that the present aggregate amount of securities in the System open market account shall not be increased or decreased by more than \$250,000,000 prior to the next meeting of the Federal Open Market Committee. The character and maturities of the securities acquired or sold shall be determined by the executive committee in the light of current market developments."

Mr. Broderick moved that the resolution be adopted in the form set forth above. Mr. Broderick's motion was seconded by Mr. Peyton.

Mr. Harrison moved to amend the resolution by striking out the requirement that a minimum amount of securities be purchased during the week beginning April 5, 1937. In this connection he pointed out that he had proposed a resolution granting discretionary authority to the

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executive committee but without a clause prescribing a mandate to buy. Mr. Sinclair seconded Mr. Harrison's motion.

Mr. Harrison's motion was put by the chair and lost, the members voting as follows:
"Aye" - Messrs. Harrison, Sinclair and Szymczak;
"No" - Messrs. Eccles, Broderick, McKee, Ransom, Davis, McKinney, Martin and Peyton.

Mr. Broderick's motion was then put by the chair and carried unanimously.

After some discussion Messrs. Ransom, Goldenweiser, Wyatt and Thurston were requested to prepare a draft of a press statement for consideration by the Committee. The individuals named withdrew from the meeting and upon their return submitted a draft of statement which was discussed and amended to read as follows:

"With a view (1) to exerting its influence toward orderly conditions in the money market and (2) to facilitating the orderly adjustment of member banks to the increased reserve requirements effective May 1, 1937, the Open Market Committee of the Federal Reserve System is prepared to make open market purchases of United States Government securities for the account of the Federal reserve banks in such amounts and at such times as may be desirable. This purpose is in conformity with the policy announced by the Board of Governors of the Federal Reserve System in its statement on January 30, 1937, which declared, with reference to the increase in reserve requirements, that by this action the System would be placed in a position where such reduction or expansion of member bank reserves as may be deemed in the public interest may be effected through open market operations."

Mr. Ransom moved that the statement as amended be approved for immediate release.

Mr. Harrison raised a question whether any statement should be issued at this time and all of the members, with the exception of Messrs. Harrison and Peyton, agreed that a public statement should be made. Mr. Peyton said he would have no objection to an explanation

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being given at the time of the publication of the weekly statement of condition of Federal reserve banks of any change in the System portfolio but that he felt a statement at this time would be misinterpreted.

Mr. McKee moved as a substitute for Mr. Ransom's motion that the following statement be released to the press:

"The Federal Open Market Committee voted today to increase its portfolio to assist in an orderly Government bond market."

The substitute motion was seconded by Mr. Davis.

The substitute motion was put by the chair and lost, the members voting as follows: "Aye" - Messrs. McKee and Davis; "No" - Messrs. Eccles, Harrison, Broderick, Szymczak, Ransom, Sinclair, McKinney, Martin and Payton.

Mr. Ransom's motion was then put by the chair and carried, Mr. McKee voting "no".

Upon motion duly made and seconded, and by unanimous vote, the readjustment of the participations of the Federal reserve banks in the System open market account as of April 1, 1937, in accordance with the plan and procedure previously followed, was approved, ratified and confirmed.

Mr. Burgess stated that in connection with the adjustment some of the Federal reserve banks had called attention to the fact that the readjusted participations showed some depreciation and that while it was small at the present time they wished to serve notice that if the depreciation in the account increases they would wish to have a reconsideration of the entire matter of readjustment of participations before the next quarterly readjustment date.

During yesterday's session, Mr. Burgess, as manager of the System open market account, had handed to the members of the Federal

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Open Market Committee a report prepared by the Federal Reserve Bank of New York of open market operations since the meeting of the Committee on January 26, 1937, which operations had been reported in detail in the usual weekly reports.

Upon motion duly made and seconded, and by unanimous vote, the transactions referred to in the report were ratified unanimously.

It was suggested that, as the Committee had granted authority to the executive committee to make such purchases or sales in the System open market account as may be necessary with a view to preserving an orderly market, and that, while authority should be given to replace maturing securities and to make such shifts in the account as may be necessary in the proper administration of the account, it would be advisable not to authorize the reduction of the amount of securities held in the account with maturities within two years to less than \$1,000,000,000. It was pointed out that the amount of securities in the account at the present time with maturities within two years was in excess of \$1,100,000,000.

Upon motion duly made and seconded, and by unanimous vote, the Committee instructed the executive committee to direct the replacement of maturing securities in the System open market account with other Government securities and to make such shifts between maturities in the account as may be necessary in the proper administration of the account, provided that the amount of securities maturing within two years be maintained at not less than \$1,000,000,000 and that the amount of bonds having maturities in excess of five years be not over \$850,000,000 nor less than \$500,000,000.

It was also agreed unanimously that, inasmuch as authority had been granted to the executive committee to increase or decrease the account, a renewal of the authority granted at previous meetings of the Committee to permit fluctuations in the account was not now necessary.

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Thereupon the meeting adjourned.

Chester Morie
Secretary.

Approved:

W. Stiles
Chairman.