

# MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

May 18, 1947

The second statutory meeting of the Federal Advisory Council for 1947 was convened in Room 928 of the Mayflower Hotel, Washington, D.C., on Sunday, May 18, 1947, at 2:10 P.M., the President, Mr. Brown, in the Chair.

## Present:

Mr. Walter S. Bucklin (alternate for Mr. Charles E. Spencer, Jr.)	District No. 1
Mr. John C. Traphagen (alternate for Mr. W. Randolph Burgess)	District No. 2
Mr. David E. Williams	District No. 3
Mr. John H. McCoy	District No. 4
Mr. Robert V. Fleming	District No. 5
Mr. J. T. Brown	District No. 6
Mr. Edward E. Brown	District No. 7
Mr. James H. Penick	District No. 8
Mr. Henry E. Atwood	District No. 9
Mr. James M. Kemper	District No. 10
Mr. Ed H. Winton	District No. 11
Mr. Reno Odlin	District No. 12
Mr. Herbert V. Prochnow	Acting Secretary.

## Absent:

Mr. Charles E. Spencer, Jr.	District No. 1
Mr. W. Randolph Burgess	District No. 2

The Council considered the question of what policies should be pursued by American commercial banks in making loans on foreign owned gold. There was also some discussion regarding the participation of American commercial banks in transactions in gold against dollars at premium prices in foreign countries.

There was a lengthy discussion regarding general business conditions and demands for credit.

The Council considered the question of whether it would be advisable to reduce the present margin requirements on security loans.

A lengthy discussion took place regarding bank holding company bill S. 829.

The meeting adjourned at 6:42 P.M.

HERBERT V. PROCHNOW  
Acting Secretary.

# MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

May 19, 1947

At 10:00 A.M., the Federal Advisory Council reconvened in Room 932 of the Mayflower Hotel, Washington, D.C.

Present: Mr. Edward E. Brown, President; Messrs. Walter S. Bucklin, John C. Traphagen, David E. Williams, John H. McCoy, Robert V. Fleming, J. T. Brown, James H. Penick, Henry E. Atwood, James M. Kemper, Ed H. Winton, Reno Odlin, and Herbert V. Prochnow, Acting Secretary.

Absent: Mr. Charles E. Spencer, Jr., and Mr. W. Randolph Burgess.

The Council reviewed its conclusions of the previous day regarding the various items on the agenda. The Council then sent a memorandum, listing the items on the agenda with the conclusions reached by the Council on each item, to the Secretary of the Board of Governors at 11:58 A.M. on May 19, 1947. The memorandum follows on pages 17, 18 and 19.

The meeting adjourned at 11:43 A.M.

HERBERT V. PROCHNOW  
Acting Secretary.

CONFIDENTIAL

MEMORANDUM TO THE BOARD OF GOVERNORS FROM THE FEDERAL  
ADVISORY COUNCIL RELATIVE TO THE AGENDA FOR THE JOINT MEET-  
ING ON MAY 20, 1947

1. What policies should be pursued by American commercial banks in making or participating in loans on foreign-owned gold? It is believed that such loans should not be made if they appear to be sought for predominantly speculative purposes, and that in any case they should be limited to an initial period of 12 months, subject to renewal, in order to provide opportunity for periodic review. What are the views of the Council?

The Council does not believe that American commercial banks should be restricted in making or participating in loans on foreign-owned gold, either in relation to the purposes for which the loans are made or the length of time for which the loans are extended.

2. It is reported that some American commercial banks have participated in transactions in gold against dollars at premium prices in foreign countries. It is believed, from the standpoint of national policy, that such transactions are undesirable and that American commercial banks should be requested to refrain from engaging in them. Does the Council agree?

The Council believes that such transactions in gold against dollars at premium prices in foreign countries may be undesirable. However, the Council believes that no action of the Federal Reserve Banks to restrict these transactions should go further than a request to refrain from engaging in them.

3. In view of the current business situation, the Board would be interested in receiving information from the Council as to whether banks generally expect a continuing strong demand for business loans, for loans secured by real estate, and for consumer credit; what effects the inventory and price situation are having upon the loan positions and policies of banks; and whether, in the various districts, there has been any general tendency for banks to follow more restrictive loan policies, for loan rates to rise, or for borrowers to request renewals of loans more frequently. In addition, the Board would be glad to have any general views which the Council might wish to express.

The Council believes it best to state its conclusions regarding this item on the Agenda in connection with the specific questions which have been raised as follows:

- (A) Do banks expect a continuing strong demand for business loans?
  - (a) The majority of the members of the Council expect a continuing good demand for business loans, but there were three members who reported some leveling off in the demand. Those who are extending term credits expect a continuing strong demand.
- (B) Do banks expect a continuing strong demand for loans secured by real estate?
  - (b) A continuing strong demand for real estate loans is anticipated, but owing to the excessive cost of new construction a lessened demand is expected for loans for new buildings.

- (C) Do banks expect a continuing strong demand for consumer credit?
- (c) All banks making such loans, as well as banks extending credit to finance companies, are experiencing a strong and increasing demand.
- (D) What effects are the inventory and price situations having upon the loan positions and policies of banks?
- (d) In general, the members of the Council report a more cautious approach to lending policies. There are some lines of business in which frozen situations appear to be developing.
- (E) Is there any tendency for loan rates to rise or for borrowers to request renewals of loans more frequently?
- (e) There has been no tendency for rates on national names of the highest credit to rise above the  $1\frac{1}{2}$  per cent rate which has prevailed, but rates for loans to smaller concerns and credits not of the highest grade have tended to rise somewhat. Rates on term loans in the last year have perhaps increased about  $\frac{1}{4}$  of 1 per cent.

Borrowers are requesting renewals of loans more frequently because of large receivables and inventories.

4. Would it be advisable to reduce the present margin requirements on security loans?

This item was not on the Agenda originally submitted to the Board for this meeting. The Council believes that a reduction in margin requirements is desirable at this time. The stock market is in a deflationary phase. It is very thin and price fluctuations are wide. There is in the opinion of the Council no danger that a reduction in margins would have any dangerous inflationary effect, or cause any considerable demand for credit, but it would operate to lessen wide fluctuations in stock prices. The Council would not favor a reduction in required margins below 50 per cent, but it believes the present 75 per cent requirement is too high.

5. At the last meeting it was understood that the Council would give further consideration to the holding company bill S. 829 and that at the next meeting it would submit its views with respect to the proposed legislation.

The Council is familiar with the holding company bill introduced in the Senate, S. 829. It understands this bill is shortly to be rewritten, and that the rewritten bill to be substituted for Senate bill 829 will follow the general lines of that bill. Obviously, the Council can not approve a bill which it has not yet seen and which has not been introduced. However, (1) it believes that holding company legislation is desirable at this time; (2) it approves the general approach to the holding company problem embodied in Senate bill 829; and (3) it believes that the new bill should contain:

- (a) A more definite statement of the objectives of the bill and of standards for Federal Reserve Board action. The incorporation in the bill of objectives and standards along the lines suggested in the recent report of a Committee of the Association of Reserve City Bankers would meet the Council's approval.

- (b) Simple justice requires that if holding companies are required to divest themselves of non-banking assets, they should be granted tax exemption in connection with such divestment. A precedent exists for this in the utility holding company legislation.
- (c) A larger percentage of ownership of stock in two or more banks than 10 per cent should be required to automatically create a holding company relationship.
- (d) There should be provisions that incidental ownership of bank stocks in fiduciary capacities such as executor, trustee under a will, etc., should not create a holding company relationship.

The Council urges the rewriting and introduction of the new bill as promptly as possible.

MINUTES OF THE MEETING OF THE FEDERAL ADVISORY COUNCIL

May 19, 1947

At 2:00 P.M., the Federal Advisory Council reconvened in the Board Room of the Federal Reserve Building, Washington, D.C., the President, Mr. Brown, in the Chair.

Present: Mr. Edward E. Brown, President; Messrs. Walter S. Bucklin, John C. Traphagen, David E. Williams, John H. McCoy, Robert V. Fleming, J. T. Brown, James H. Penick, Henry E. Atwood, James M. Kemper, Ed H. Winton, Reno Odlin, and Herbert V. Prochnow, Acting Secretary.

Absent: Mr. Charles E. Spencer, Jr., and Mr. W. Randolph Burgess.

Mr. Ralph A. Young, Assistant Director of the Division of Research and Statistics of the Federal Reserve System spoke on the subject "Credit, Monetary and Fiscal Prospects, 1947-48."

The meeting adjourned at 3:15 P.M.

HERBERT V. PROCHNOW  
Acting Secretary.

MINUTES OF JOINT CONFERENCE OF THE FEDERAL ADVISORY COUNCIL  
AND THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

May 20, 1947

At 10:45 A.M., a joint conference of the Federal Advisory Council and the Board of Governors of the Federal Reserve System was held in the Board Room of the Federal Reserve Building, Washington, D.C.

Present: Members of the Board of Governors of the Federal Reserve System:

Chairman Marriner S. Eccles; Governors M. S. Szymczak, Ernest G. Draper, R. M. Evans and Lawrence Clayton; also, S. R. Carpenter, Secretary of the Board of Governors, and J. Leonard Townsend, Assistant General Counsel of the Board of Governors.

Present: Members of the Federal Advisory Council:

Mr. Edward E. Brown, President; Messrs. Walter S. Bucklin (alternate for Charles E. Spencer, Jr.), John C. Traphagen (alternate for W. Randolph Burgess), David E. Williams, John H. McCoy, Robert V. Fleming, J. T. Brown, James H. Penick, Henry E. Atwood, James M. Kemper, Ed H. Winton, Reno Odlin, and Herbert V. Prochnow, Acting Secretary.

There was a discussion regarding the policies which should be pursued by American commercial banks in making or participating in loans on foreign-owned gold. The President of the Council stated that the Council does not believe American commercial banks should be restricted in making or participating in loans on foreign-owned gold, either in relation to the purposes for which the loans are made or the length of time for which the loans are extended.

The Board of Governors had previously advised the Council that some American commercial banks had participated in transactions in gold against dollars at premium prices in foreign countries. The Board asked the opinion of the Council regarding these practices. The President of the Council stated that the Council believes such transactions in gold against dollars at premium prices in foreign countries may be undesirable. However, it was the opinion of the Council that no action by the Federal Reserve banks to restrict these transactions should go further than a request to refrain from engaging in them.

There was a general discussion regarding economic conditions and the demand for bank credit, as well as a discussion of the present margin requirements on security loans. The President of the Council stated that the Council believes a reduction in margin requirements is desirable at this time. The Council does not favor a reduction in required margins below 50 per cent, but it believes the present 75 per cent requirement is too high.

There was a long discussion regarding bank holding company bill S. 829. The conclusions of the Council on this bill are expressed on pages 18 and 19 of these minutes.

The meeting adjourned at 1:30 P.M.

HERBERT V. PROCHNOW  
Acting Secretary.

# MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

May 20, 1947

At 2:45 P.M., the Federal Advisory Council reconvened in the Board Room of the Federal Reserve Building, Washington, D.C., the President, Mr. Brown, in the Chair.

Present: Mr. Edward E. Brown, President; Messrs. Walter S. Bucklin (alternate for Charles E. Spencer, Jr.), John C. Traphagen (alternate for W. Randolph Burgess), David E. Williams, John H. McCoy, Robert V. Fleming, J. T. Brown, James H. Penick, Henry E. Atwood, James M. Kemper, Ed H. Winton, Reno Odlin, and Herbert V. Prochnow, Acting Secretary.

Absent: Mr. Charles E. Spencer, Jr., and Mr. W. Randolph Burgess.

The Council approved the resolution and memorandum which follow, together with the accompanying letter of transmittal from President Brown:

## RESOLUTION

The Council for the past few years has at almost every meeting discussed the holding company situation, the inadequacies of existing legislation, and proposals for additional legislation in connection with it.

(1) The Council believes that holding company legislation should be enacted at this time. Experience has shown that the present legislation is inadequate and that additional legislation is urgently necessary.

(2) It approves the general approach to the holding company problem embodied in Senate Bill 829.

(3) It believes Senate Bill 829 should be amended —

(a) By adding to the declaration of policy and the standards for Federal Reserve Board, Comptroller of the Currency, and Federal Deposit Insurance Corporation action a more definite statement of objectives and standards. (A memorandum is attached which was the subject of discussion between the Board of Governors and the Federal Advisory Council which indicates the type of amendments in this regard which the Council believes necessary.)

(b) By granting tax exemption to such holding companies as are required to divest themselves of non-banking assets. Simple justice requires that such tax exemption should be granted, and a precedent exists for it in the utility holding company legislation.

(c) By requiring a larger percentage than 10 per cent of the ownership of stock in two or more banks in order to create an automatic holding company relationship.

(d) By providing that incidental ownership of bank stocks in fiduciary capacities such as executor, trustee under a will, etc., should not create an automatic holding company relationship.

The Council urges the Board to submit amendments in accordance with these suggestions and to press for the enactment of the bill as so amended.

May 20, 1947.

MEMORANDUM

1. To reach and regulate any banking operation which, functioning in an area or with a structure larger than that permitted to independent banks, can or does, through the medium of concentrated control, jeopardize independent competitive banking at local or regional levels or place independent banks under the particular circumstances at a competitive disadvantage;
2. To confine the size and expanse of any such banking operation, regardless of its competitive or other aspects, within limits consistent with adequate and sound banking; and
3. To control the magnitude and expanse of any such banking operation, regardless of all other considerations, to the end that, in the event of adverse general economic conditions, such an operation will not be subjected to an inordinate pressure arising from unwieldiness due solely to mere size and expanse which, in turn, may put an inordinate pressure on the nation's banking structure.

May 20, 1947

Honorable Marriner S. Eccles, Chairman  
Board of Governors,  
Federal Reserve System  
Washington 25, D.C.

Dear Chairman Eccles:

Transmitted herewith is resolution of the Federal Advisory Council passed at its meeting today.

Very truly yours,

(Signed) Edward E. Brown, President,  
Federal Advisory Council.

[Enclosures]

The meeting adjourned at 3:30 P.M.

HERBERT V. PROCHNOW  
Acting Secretary.

NOTE: This transcript of the Acting Secretary's notes is not to be regarded as complete or necessarily entirely accurate. The transcript should be considered as being strictly for the sole use of the members of the Federal Advisory Council.

H. V. P.

The Acting Secretary's notes on the meeting of the Federal Advisory Council on May 18, 1947, at 2:10 P.M., in Room 928 of the Mayflower Hotel, Washington, D. C.

All members of the Federal Advisory Council were present except Mr. Charles E. Spencer, Jr., for whom Mr. Walter S. Bucklin served as an alternate, and Mr. W. Randolph Burgess, for whom Mr. John C. Traphagen served as an alternate.

Because of transportation difficulties, Mr. Penick and Mr. Atwood arrived after the meeting had started.

WHAT POLICIES SHOULD BE PURSUED BY AMERICAN COMMERCIAL BANKS IN MAKING OR PARTICIPATING IN LOANS ON FOREIGN-OWNED GOLD? IT IS BELIEVED THAT SUCH LOANS SHOULD NOT BE MADE IF THEY APPEAR TO BE SOUGHT FOR PREDOMINANTLY SPECULATIVE PURPOSES, AND THAT IN ANY CASE THEY SHOULD BE LIMITED TO AN INITIAL PERIOD OF 12 MONTHS, SUBJECT TO RENEWAL, IN ORDER TO PROVIDE OPPORTUNITY FOR PERIODIC REVIEW. WHAT ARE THE VIEWS OF THE COUNCIL?

E. E. Brown comments that the central banks of foreign countries sometimes fail to show in their reserve position that gold has been pledged against a loan. While this is bad banking practice, it is no worse for the commercial banks than it is for the Federal Reserve banks to make loans to foreign central banks which fail to show in their reserve position that gold has been pledged. Brown states that there is also some criticism that any country which borrows dollars on gold rather than selling the gold outright is placing itself in a position to profit from an increase in the dollar price of gold. However, by lending against gold, we tend to discourage the idea that there is a prospect of devaluation.

Fleming mentions that the bank examiners criticised the participation of his bank in a loan to the Netherlands.

Traphagen sees no reason why commercial banks should be prevented from loaning on gold.

J. T. Brown assumes from the memorandum of the staff of the Board of Governors that the essential part of the discussion hinges on the fact that the foreign countries borrow dollars against gold rather than to sell the gold outright, and they thereby place themselves in a position to profit from an increase in the dollar price of gold.

E. E. Brown asks the various members of the Council whether they are in favor of restricting American commercial banks in making or participating in loans on foreign-owned gold, either in relation to the purposes for which the loans are made or the length of time for which the loans are extended. All the members of the Council are against restricting American commercial banks in this manner.

Odlin. It seems impossible to believe anyone is even thinking of devaluation in view of the fact that we bought that bill of goods once.

Fleming. It seems fantastic.

IT IS REPORTED THAT SOME AMERICAN COMMERCIAL BANKS HAVE PARTICIPATED IN TRANSACTIONS IN GOLD AGAINST DOLLARS AT PREMIUM PRICES IN FOREIGN COUNTRIES. IT IS BELIEVED, FROM THE STANDPOINT OF NATIONAL POLICY, THAT SUCH TRANSACTIONS ARE UNDESIRABLE AND THAT AMERICAN COMMERCIAL BANKS SHOULD BE REQUESTED TO REFRAIN FROM ENGAGING IN THEM. DOES THE COUNCIL AGREE?

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E. E. Brown asks Traphagen to comment on this item.

Traphagen states that Sproul told him it is bad to have the American dollar quoted at a discount and Sproul also said it encourages people in foreign countries to use their dollars to buy gold instead of goods and services from us.

E. E. Brown. In Mexico the Government thought that the best way to get the people to have confidence in their currency was to offer gold for sale freely. Consequently, Mexico sells gold. An American may buy gold in Mexico and take it to Hong Kong or some other place to sell it. To the extent that dollars go into gold illegally, the foreign country is deprived of dollars to buy our goods and services. Brown believes the Federal Reserve banks should discourage this practice, but he questions whether the United States should try to police this situation in all foreign countries. Brown explains also how American travellers in France may exchange their travellers' checks for French francs in the black market. The Frenchman may smuggle the travellers' checks into another country and obtain gold. It is impossible for American banks to police every type of transaction abroad that may be illegal.

Fleming assumes that some special legislation might be required and he does not believe this is possible.

Traphagen asks whether it would not be sufficient, simply to have the Federal Reserve banks ask banks engaging in these transactions to refrain from participating in them.

Winton comments that when you start controlling every detail in the life of American citizens and their activities in foreign countries you have a real job.

E. E. Brown states that such transactions in gold against dollars at premium prices in foreign countries may be undesirable. However, he says he will tell the Board it is the Council's view that no action of the Federal Reserve banks to restrict these transactions should go further than a request to refrain from engaging in them. All of the members of the Council agree with this viewpoint.

IN VIEW OF THE CURRENT BUSINESS SITUATION, THE BOARD WOULD BE INTERESTED IN RECEIVING INFORMATION FROM THE COUNCIL AS TO WHETHER BANKS GENERALLY EXPECT A CONTINUING STRONG DEMAND FOR BUSINESS LOANS, FOR LOANS SECURED BY REAL ESTATE, AND FOR CONSUMER CREDIT; WHAT EFFECTS THE INVENTORY AND PRICE SITUATION ARE HAVING UPON THE LOAN POSITIONS AND POLICIES OF BANKS; AND WHETHER, IN THE VARIOUS DISTRICTS, THERE HAS BEEN ANY GENERAL TENDENCY FOR BANKS TO FOLLOW MORE RESTRICTIVE LOAN POLICIES, FOR LOAN RATES TO RISE, OR FOR BORROWERS TO REQUEST RENEWALS OF LOANS MORE FREQUENTLY. IN ADDITION, THE BOARD WOULD BE GLAD TO HAVE ANY GENERAL VIEWS WHICH THE COUNCIL MIGHT WISH TO EXPRESS.

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E. E. Brown believes it would be better to discuss this item by considering separately the specific questions which have been raised, and he asks how many members expect a continuing strong demand for business loans. The majority of the members of the Council expect a continuing good demand for business loans, but there were three members who reported some levelling off in the demand. Those granting term loans expect a continuing strong demand.

Fleming remarks that medium-sized firms are asking for term loans.

Odlin thinks the demand will continue strong.

J. T. Brown agrees.

Bucklin thinks the demand will be good but perhaps not strong.

Williams reports a good demand but some levelling off.

McCoy states that many small banks are well loaned up. He also reports that there are more loans for periods of five to ten days for the purpose of taking discounts.

Winton states they have had only one request for a term loan recently and other loans are tapering off somewhat.

Kemper reports a good demand for the period immediately ahead and anticipates large crop loans.

Traphagen states there is a levelling off of ordinary loans, but there is a rather strong demand for term loans.

E. E. Brown asks whether the members of the Council expect a continuing strong demand for loans secured by real estate.

Fleming expects a strong demand.

E. E. Brown states that the increases in the Chicago area may look large but that is due to the fact that the figures previously were small.

Traphagen reports that the demand is not increasing.

Winton says they do not like real estate loans but the demand is heavy.

McCoy states that his community is short about three thousand houses. One of their builders has dug 164 basements in one week and 157 in another week. The insurance companies will probably take most of the loans.

Kemper reports that in the Tenth district they do not expect as strong a demand because building is slowing down.

Odlin expects a slowing up.

E. E. Brown. Prospective buyers of homes are refusing to pay \$10,000 for houses that would normally sell for \$3,000 to \$4,000. There is a great unsatisfied demand for housing but high building costs are tending to slow down demands for real estate loans.

J. T. Brown believes there is a slackening in construction. His bank never was interested in the inflationary real estate loans and these loans tend to go to insurance companies.

Fleming reports that insurance companies tend to take the loans his bank will not take. The demand continues strong.

E. E. Brown states that it is apparently the view of the Council that there will be a continuing strong demand for real estate loans, but most of these loans may move to other institutions such as insurance companies.

Traphagen reports that the large insurance companies are discontinuing major housing projects because of high building costs.

E. E. Brown asks whether banks expect a continuing strong demand for consumer loans. All of the members of the Council anticipate a continuing strong demand for such loans as well as a heavy demand from finance companies. Brown also asks what effect the inventory and price situations are having upon the loan positions and policies of banks. He states from his observation that the younger officers are beginning to see some of the problems which develop with frozen situations and are realizing the need for caution.

Bucklin. The young officers are beginning to see the necessity for more care in making loans.

Traphagen reports that there is more caution in lending policies and that some loans may develop into frozen situations.

McCoy reports that no loans are frozen yet.

Williams agrees with Traphagen that caution in lending has developed and that there is some tendency for freezing in certain lines.

Fleming reports no freezing yet but that generally speaking banks are becoming more cautious.

Kemper. Some soft spots are showing up in industries which grew out of the war and those facing severe competitive conditions.

Winton states he has had a little problem in the past in selling some of his younger officers on the need for careful credit policies but they are now telling him they realize the soundness of his advice.

Odlin. The warning regarding inventory problems probably came early enough to lead many businessmen to watch their inventories more carefully. The frozen food situation is one of the bad spots.

J. T. Brown. The inventory question is receiving careful consideration now, but the warning regarding inventories was probably given early enough to prevent serious trouble. Some lumber concerns are having difficulties.

E. E. Brown. There are no failures of any size in the Seventh district. A number of freezes are in sight with possible losses to banks. Metal manufacturers are among those having trouble.

Odlin. The lumber companies on the Pacific Coast that cut a good grade of lumber are not having trouble.

E. E. Brown asks whether there is any tendency in the various districts for loan rates to rise or for borrowers to request renewals of loans more frequently. He states that from his observation there is no

tendency for rates on national names of the highest grade to rise above the 1 1/2% rate which has prevailed. However, rates for loans to smaller concerns and credits not of the highest grade have tended to rise somewhat. Rates on term loans in the last year have perhaps increased about 1/4 of 1 per cent. Borrowers are requesting renewals of loans more frequently because of large receivables and inventories. All the members of the Council agree that this summary is an accurate statement of the situation.

WOULD IT BE ADVISABLE TO REDUCE THE PRESENT MARGIN REQUIREMENTS ON SECURITY LOANS?

Fleming states that the question of margin requirements was not on the agenda and asks whether the Council believes the question should be raised with the Board.

Williams comments that the Board knows how the Council feels on the question.

Traphagen states that Eccles told him that until there was a deflationary period he would not consider lowering the margin requirements. However, Traphagen thinks it would be desirable to raise the question with the Board.

E. E. Brown believes the 75 per cent margin requirement is an improper use of power by the Board.

Bucklin. Eccles is in favor of making our security market an investment market rather than a speculative market. The English market is more of an investment market.

Fleming. Emil Schram wants a conservative market too, but the market is very thin because of margin requirements.

E. E. Brown states that the market is very thin and there are wide price fluctuations. There are evidences that the stock market is in a deflationary phase. He would not favor a reduction in the required margin below 50 per cent, but he believes the present 75 per cent requirement is too high.

Odlin thinks that a reasonable amount of credit should be permitted to enter the market.

E. E. Brown asks whether the members of the Council wish to raise the question with the Board of reducing the present margin requirements. All of the members of the Council are in favor of discussing the matter with the Board. (Penick and Atwood, who had been delayed by transportation difficulties, entered the meeting at 4:40 P.M.)

AT THE LAST MEETING IT WAS UNDERSTOOD THAT THE COUNCIL WOULD GIVE FURTHER CONSIDERATION TO THE HOLDING COMPANY BILL S. 829 AND THAT AT THE NEXT MEETING IT WOULD SUBMIT ITS VIEWS WITH RESPECT TO THE PROPOSED LEGISLATION.

E. E. Brown reports that the American Bankers Association decided to stay out of the discussion of this issue, but that the Association of Reserve City Bankers has given consideration to the problem. A Committee of the Association of Reserve City Bankers has made a rather exhaustive survey and study of the subject. Copies of the report of the Association of Reserve City Bankers have been given to the members of the Council. This is the final report, with the exception perhaps of one or two minor word changes. Copies of the final mimeograph report of the Association of Reserve City Bankers will be sent to the Board of Governors, to the Chairmen of the Committees on Banking and Currency in the Senate and House, to the members of the Association of Reserve City Bankers, and other interested groups. It is Brown's understanding that the tax free provision is agreeable to Eccles, but that Eccles believes this is a matter for the Treasury to consider. Until the Treasury gives its approval, Eccles does not wish to include a provision in the bill covering matters which are the responsibility of the Treasury.

Bucklin believes some legislation is desirable, but has not had time to study the memorandum of the Reserve City Bankers.

E. E. Brown thinks there may be a 50-50 opportunity of getting a bill along these general lines through Congress. If the Council takes a position supporting the conclusions of the Reserve City Bankers as they were approved at the recent Swampscott meeting, it will indicate clearly to Congress and to the banking authorities the viewpoint of bankers generally on this important subject.

Fleming thinks that Brown has stated the matter clearly and he agrees that the subject has been thoroughly thrashed over.

E. E. Brown states that in his judgment a figure higher than 10 per cent, possibly around 20 per cent, of ownership of stock in two or more banks, should be required to create an automatic holding company relationship. Brown understands an agreement has been reached regarding casual relationships such as trust department situations.

Fleming thinks the holding companies would be better off dealing with Snyder and Wiggins than with some individuals in the future whose views are not known.

Kemper has nothing further to add to the discussion.

McCoy asks what limitations there are regarding the acquisition of more banks.

E. E. Brown states that approval must be obtained. Brown also reads the three essential goals of the legislation as listed in the memorandum of the Reserve City Bankers. (A copy of the report of the Association of Reserve City Bankers is attached to these minutes.)

Odlin states that the independent bankers believe that the report of the Reserve City Bankers may have helped clarify the proposed legislation.

McCoy thinks that the bill might be better if it further strengthened the rights of independent banks.

E. E. Brown states that the Reserve City memorandum is meant to be more restrictive than the original bill, S. 829.

Odlin agrees with McCoy that it is desirable to strengthen the rights of independent banks so far as that is possible, but that no legislation can cover all the problems of competitive situations.

Atwood states that his group would support the bill with the proposals set up in the Reserve City memorandum prepared at the recent meeting at Swampscott.

E. E. Brown advises that Julian Baird told him yesterday (May 17, 1947) that they were in favor of the bill with the Swampscott proposals incorporated.

Bucklin. We are in favor of legislation.

(Fleming leaves the meeting at 6:00 P.M.)

E. E. Brown. There has never been such general agreement as now on the various aspects of bank holding company legislation.

Penick states that he has not spoken on the legislation because they do not have this problem in his district.

Winton reports that they do not have holding companies in Texas. He says frankly that he is opposed to holding companies. At one time he was with a bank having over 30 branches, and he felt there was too much power concentrated in a few hands.

Odlin asks whether the Council could not go on record approving the proposed bank holding company legislation if the present bill is rewritten to include the suggestions incorporated in the memorandum of the Association of Reserve City Bankers, which memorandum was approved at the Swampscott meeting of the Association.

E. E. Brown. The Council could say that it concurs in the principles embodied in the report of the Committee on Federal Relationships of the Association of Reserve City Bankers, of which five members of the present Council were members; and the Council could recommend that the present bill be modified in accordance with the Swampscott proposals, particularly to include the three essential goals listed in the Swampscott memorandum. The bill should be amended to provide:

- (1) That enforced liquidation of outside assets should be tax free;
- (2) That automatic coverage should be changed from 10 per cent to 20 per cent; and
- (3) That provision should be made to insure that incidental ownership such as that in trust departments should not create an automatic holding company relationship.

Williams asks the members of the Council if they would vote for the legislation if there were no situation on the Pacific Coast. In response to Williams' question a number of members replied that they would vote in favor of such legislation.

E. E. Brown states that the Council may advise the Board that it approves the general approach to the holding company problem embodied in Senate Bill 829 but believes that there should be incorporated in the bill objectives and standards along the lines suggested in the recent report of the Committee on Federal Relationships of the Association of Reserve City Bankers. Five present members of the Council and six former members of the Council were on the Committee of sixteen bankers who constituted the Reserve City Committee.

Winton wishes to give the matter a little more thought.

McCoy is in favor of the bill including the proposals by the Reserve City Committee, but he believes that perhaps the bill should have more restrictions.

J. T. Brown agrees with the Reserve City proposals and believes they make the bill more restrictive. Sooner or later we shall get legislation, and it could easily be worse than is now being proposed.

E. E. Brown states that the Council could report to the Board that the Council is familiar with the bank holding company bill, S. 829. It understands this bill is shortly to be rewritten, and that the rewritten bill to be substituted for Senate Bill 829 will follow the general lines of that bill. Obviously, the Council cannot approve a bill which it has not yet seen and which has not been introduced. However, (1) it believes that holding company legislation is desirable at this time; (2) it approves the general approach to the holding company problem embodied in Senate bill 829; and (3) it believes that the new bill should contain a more definite statement of the objectives of the bill and of standards for Federal Reserve Board action. The incorporation in the bill of objectives and standards along the lines suggested in the recent report of a Committee of the Association of Reserve City Bankers would meet the Council's approval. The Council could also report that of the sixteen members constituting the Committee on Federal Relationships of the Association of Reserve City Bankers five were present members of the Federal Advisory Council and six were former members.

Odlin moves that the Council express itself as in agreement with the summary presented by E. E. Brown, and all members of the Council agree.

The meeting adjourned at 6:42 P.M.

The Council reconvened at 10:00 A.M. on May 19, 1947, in Room 932 of the Mayflower Hotel, Washington, D. C.

All members of the Council were present except Mr. Charles E. Spencer, Jr., for whom Mr. Walter S. Bucklin served as an alternate, and Mr. W. Randolph Burgess, for whom Mr. John C. Traphagen served as an alternate.

The Council approved the attached memorandum, which it prepared, to be sent to the Board of Governors relative to the agenda for the joint meeting of the Board and the Council on May 20, 1947. The memorandum was delivered to the Secretary of the Board of Governors at 11:58 A.M. on May 19, 1947. It will be noted that each item of the agenda is listed with the comments of the Council on the item.

The meeting adjourned at 11:43 A.M.

CONFIDENTIAL

MEMORANDUM TO THE BOARD OF GOVERNORS

FROM THE

FEDERAL ADVISORY COUNCIL

RELATIVE TO THE AGENDA FOR THE JOINT MEETING

ON MAY 20, 1947

1. What policies should be pursued by American commercial banks in making or participating in loans on foreign-owned gold? It is believed that such loans should not be made if they appear to be sought for predominantly speculative purposes, and that in any case they should be limited to an initial period of 12 months, subject to renewal, in order to provide opportunity for periodic review. What are the views of the Council?

The Council does not believe that American commercial banks should be restricted in making or participating in loans on foreign-owned gold, either in relation to the purposes for which the loans are made or the length of time for which the loans are extended.

2. It is reported that some American commercial banks have participated in transactions in gold against dollars at premium prices in foreign countries. It is believed, from the standpoint of national policy, that such transactions are undesirable and that American commercial banks should be requested to refrain from engaging in them. Does the Council agree?

The Council believes that such transactions in gold against dollars at premium prices in foreign countries may be undesirable. However, the Council believes that no action of the Federal Reserve Banks to restrict these transactions should go further than a request to refrain from engaging in them.

3. In view of the current business situation, the Board would be interested in receiving information from the Council as to whether banks generally expect a continuing strong demand for business loans, for loans secured by real estate, and for consumer credit, what effects the inventory and price situation are having upon the loan positions and policies of banks; and whether, in the various districts, there has been any general tendency, for banks to follow more restrictive loan policies, for loan rates to rise, or for borrowers to request renewals of loans more frequently. In addition, the Board would be glad to have any general views which the Council might wish to express.

The Council believes it best to state its conclusions regarding this item on the Agenda in connection with the specific questions which have been raised as follows:

- (A) Do banks expect a continuing strong demand for business loans?
  - (a) The majority of the members of the Council expect a continuing good demand for business loans, but there were three members who reported some leveling off in the demand. Those who are extending term credits expect a continuing strong demand.
- (B) Do banks expect a continuing strong demand for loans secured by real estate?
  - (b) A continuing strong demand for real estate loans is anticipated, but owing to the excessive cost of new construction a lessened demand is expected for loans for new buildings.
- (C) Do banks expect a continuing strong demand for consumer credit?
  - (c) All banks making such loans, as well as banks extending credit to finance companies, are experiencing a strong and increasing demand.
- (D) What effects are the inventory and price situation having upon the loan positions and policies of banks?
  - (d) In general, the members of the Council report a more cautious approach to lending policies. There are some lines of business in which frozen situations appear to be developing.
- (E) Is there any tendency for loan rates to rise or for borrowers to request renewals of loans more frequently?
  - (e) There has been no tendency for rates on national names of the highest credit to rise above the 1-1/2 per cent rate which has prevailed, but rates for loans to smaller concerns and credits not of the highest grade have tended to rise somewhat. Rates on term loans in the last year have perhaps increased about 1/4 of 1 per cent.

Borrowers are requesting renewals of loans more frequently because of large receivables and inventories.

- 4. Would it be advisable to reduce the present margin requirements on security loans?

This item was not on the Agenda originally submitted to the Board for this meeting. The Council believes that a reduction in margin requirements is desirable at this time. The stock market is in a deflationary phase. It is very thin and price fluctuations are wide. There is in the opinion of the Council no danger that a reduction in margins would have any dangerous inflationary effect, or cause any considerable demand for credit, but it would operate to lessen wide fluctuations in stock prices. The Council would not favor a reduction in required margins below 50 per cent, but it believes the present 75 per cent requirement is too high.

5. At the last meeting it was understood that the Council would give further consideration to the holding company bill S. 829 and that at the next meeting it would submit its views with respect to the proposed legislation.

The Council is familiar with the holding company bill introduced in the Senate, S. 829. It understands this bill is shortly to be rewritten, and that the rewritten bill to be substituted for Senate bill 829 will follow the general lines of that bill. Obviously, the Council can not approve a bill which it has not yet seen and which has not been introduced. However, (1) it believes that holding company legislation is desirable at this time; (2) it approves the general approach to the holding company problem embodied in Senate bill 829; and (3) it believes that the new bill should contain:

- (a) A more definite statement of the objectives of the bill and of standards for Federal Reserve Board action. The incorporation in the bill of objectives and standards along the lines suggested in the recent report of a Committee of the Association of Reserve City Bankers would meet the Council's approval.
- (b) Simple justice requires that if holding companies are required to divest themselves of non-banking assets, they should be granted tax exemption in connection with such divestment. A precedent exists for this in the utility company legislation.
- (c) A larger percentage of ownership of stock in two or more banks than 10 per cent should be required to automatically create a holding company relationship.

- (d) There should be provisions that incidental ownership of bank stocks in fiduciary capacities such as executor, trustee under a will, etc., should not create a holding company relationship.

The Council urges the rewriting and introduction of the new bill as promptly as possible.

The Council reconvened in the Board Room of the Federal Reserve Building at 2:00 P.M. on May 19, 1947, to hear Mr. Ralph A. Young, Assistant Director of the Division of Research and Statistics of the Federal Reserve System.

All members of the Council were present except Mr. Charles E. Spencer, Jr., for whom Mr. Walter S. Bucklin served as an alternate, and Mr. W. Randolph Burgess, for whom Mr. John C. Traphagen served as an alternate.

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E. E. Brown presents Mr. Ralph A. Young, who speaks on the subject "Credit, Monetary and Fiscal Prospects, 1947-48". A confidential copy of Mr. Young's remarks is attached.

\* \* \* \* \*

After Mr. Young's talk, the following brief discussion ensued:

E. E. Brown asks where Young obtained his figures on real estate loans.

Young replies that his figures are a composite of the judgments of various government agencies.

Fleming asks what guide Young used for obtaining his budget figures.

Young replies that he and his associates watch the proposals going through Congress. He states that in his judgment there is more likely to be an increase in the debt in the future rather than a decline. The outlook in this respect is not particularly hopeful.

Odlin asks for Young's views on bank earnings.

Young reports that the gross earnings of member banks are estimated at \$2.6 billions for 1947 compared to \$2.4 billions for 1946. Net earnings of member banks are estimated for 1947 at \$700 million compared to about \$690 million for 1946.

Bucklin asks on what basis Young estimates that there will be a moderate recession.

Young replies that at the last meeting of the Council, Thomas gave the following four reasons for expecting a recession:

- (1) The narrow margins now left to consumers after paying their expenses and taxes;
- (2) The resistance of consumers to higher prices and the decisions of consumers to defer expenditures;
- (3) The decline in the rate of expansion of business inventory; and
- (4) The fact that fiscal developments have been and may continue to be deflationary.

Young states that since that report by Thomas, three additional factors have developed:

- (1) A leveling off in business expenditures for building expansion and construction;
- (2) Some falling off in foreign demand for our products because foreign countries have been using up their dollar exchange more rapidly than anticipated; and
- (3) A contraction in business profits because of the slackening in price advances and rising wage costs.

Traphagen asks for Young's viewpoint on the outlook for agricultural prices.

Young believes agricultural prices look vulnerable. In the Staff's analysis, he states they gave emphasis to a slackening of foreign demand, but it now looks as if the demand for our agricultural products may be heavier than anticipated.

E. E. Brown reports that large concerns that expected to finance industrial expansion by stocks are now looking to banks for credit, including term loans. He states that it is possible loans may go up more than Young anticipates, but that real estate loans may not go up as much as Young expects.

Young replies that they will be willing to settle for the development Brown has mentioned.

The meeting adjourned at 3:15 P.M.

Not to be published  
or publicly quoted.

## CREDIT, MONETARY, AND FISCAL PROSPECTS, 1947-1948

Ralph A. Young\*

At the last meeting of the Council, Mr. Thomas presented an analysis of current economic tendencies and prospects for 1947-1948. His diagnosis indicated that a number of critical maladjustments were developing in the current situation of inflationary boom and over-full employment and that, in consequence, a period of recession and readjustment was likely to set in at some stage in the not too distant future. The indications available since his report lend additional support to this general view.

Mr. Thomas' report stressed that prospects pointed to what might be described as recession, but by no means depression, with the corrective period possibly having a relatively short duration. No developments have been noted since his report that would warrant a revision of this general conclusion. The science of economic projection is far from exact, however, and error is apt to be wider with regard to timing and size of change than with regard to direction of change.

The present report is a supplement to the one presented at your last meeting, but limited in focus to prospective financial tendencies. It is directed to the question: In the light of the current economic outlook for early moderate recession, what tendencies will likely characterize banking, monetary, and fiscal developments during 1947 and the early part of 1948?

### Financial Factors in Recent Inflationary Pressures

As background for our projections, the strategic forces in recent inflationary pressures need brief review. The most important of these have been the war-created backlog of domestic and foreign demand, the super-abundant bank credit and money supply expanded directly by war finance, and the further expansion of bank credit and money supply during the past year.

Because of the public's large accumulated holdings of liquid assets, consumers in 1946 were able to supplement substantially their current disposable income of nearly 150 billion dollars by spending liquid assets. The buying power added to consumption markets (including residential real estate) from this source amounted to approximately 10 billion dollars.

\*Statement before Federal Advisory Council, Washington, D. C., May 19, 1947.

Many billions more were added from consumer credit and mortgage credit sources, including banks. The active demand for consumer goods at rapidly rising prices has been sustained by these factors.

The extremely active demand from consumers within the country, combined with unprecedentedly heavy demands for manufactured goods from world markets, has encouraged manufacturing and trade enterprises to expand rapidly holdings of inventory and receivables and to spend in record volume for replacements of and additions to equipment and plant facilities. Equipment and property expenditures of railroads and public utilities have also been in heavy volume. High and rising prices relative to costs at capacity operating levels, aided by lowered tax rates on corporate income, have made for widespread profits and high levels of profitability. Under these conditions, the abnormally large business expenditures for current asset expansion and for equipment and plant have been financed largely by retained earnings and by other funds from operations. Many businesses, however, have found it necessary to draw down their war accumulated liquid asset holdings, to obtain equity capital, or to incur new debt. Business borrowing demands on banks for short and medium-term credit have been especially heavy.

Strong consumer and industrial demands for agricultural products, together with urgent demands for foods and other farm items from world markets, have raised prices of farm output above the post-World War I peak and carried agricultural income to new high levels. While farmers have spent freely for consumption goods, for farm equipment and buildings, and for land, these expenditures for the most part have been financed out of income and liquid asset holdings with expansion in debt largely limited to financing the purchase of farms or farm land. Because of their favorable income situation, total liquid asset holdings of farmers have shown continued rapid growth.

With the war-created backlog of domestic and foreign demand and a superabundant supply of money and liquid assets available for spending, capacity output has been assured at some advance in prices without further monetary expansion. Notwithstanding, expansion of the money supply held by the public continued to occur in 1946 at a rate of nearly 13 billion dollars or close to two-thirds of the wartime average annual increase, and has only recently been brought under check by seasonal and other temporary factors. About half of last year's expansion in the public's money supply represented desirable readjustment in the Treasury's position to peacetime conditions, and was brought about by the use of excess Treasury balances to retire public debt held by nonbank investors. The remaining half of the monetary increase reflected not expansion of bank loan portfolios resulting from a record demand for bank credit to finance business, to finance ownership of residential and farm properties, and to finance various consumer needs, but mainly the purchase of durable goods.

While some of the recent bank credit expansion has also increased production and in this way has helped to reduce inflationary pressures, there can be little question but that on balance the further monetary expansion has added materially to such pressures and has helped to carry the advance in prices to levels higher than otherwise would have been reached. At the same time, the bank credit and monetary expansion did not go as far as was potentially possible. It was held down in part by reduction in security loans accompanying termination of war financing, maintenance of high margin requirements, and uncertain security market conditions. Another factor was consumer credit regulation which helped to check credit demand and to maintain a high rate of repayment on outstanding consumer paper. Lastly, Treasury debt retirement, particularly of bank-held debt, contributed to a continuing moderate pressure on bank reserves and restrained additional rapid expansion of bank investment in Government securities.

#### Bank Credit and Monetary Expansion, 1947-1948

The crucial role of private credit expansion in recent monetary developments raises the question as to whether business, farm, urban real estate and consumer credit demand will continue to increase further the money supply even in the face of prospects for moderate economic recession. The current outlook is in this direction, but the pace of credit expansion will probably be at a much slower rate than during last year. The important tendencies that will likely characterize bank credit developments over the months ahead may be summarized as follows:

Business Loans: - At the end of 1946, business loans at all banks (including open-market paper but excluding loans secured by real estate) stood at 1½ billion dollars. Another billion dollars of growth was added in the first quarter, but the slackening of inflationary expansion of national product together with the outlook for recession is softening business credit demand and tightening credit availability. Close to an additional billion dollars of growth seems an outside possibility for the year, taking into account seasonal influences near the year-end. Some small net reduction in business loan outstandings will likely occur during the first half of 1948.

There are a number of uncertain factors, however, that might swell loan demand during the second half of this year. Financial readjustments, which will confront many businesses, especially small and medium-size enterprises in the face of declining sales, may bring about an unexpected volume of new borrowing. In retailing, for example, there will be increased emphasis on credit sales at a time of retarded collections, which may present problems in some cases of receivables financing, and a further rise in receivables will likely characterize manufacturing business. With declining sales, involuntary inventory accumulation by manufacturers and retailers may be a source of special credit demand. Another source of underestimate is the possible credit demand of various consumer credit agencies, such as sales finance and personal finance companies. Finally, if securities

market conditions are unfavorable, contemplated expenditures by railroads and public utilities may need to be supported by more bank financing than is now projected.

Farm Loans: - Continuing profitability of farm operations will result in little, if any, increase in farm production loans during this year. Indications from the Board's annual survey of consumer finances, made early this year, point to a moderately reduced volume of farm equipment and hence a smaller credit demand for purchase of such equipment. Some further increase may occur in the farm real estate category as a result of continuing transfers of farm property. With lower farm prices, as generally expected, borrowing for production purposes may rise during the production season in 1948, but lower farm prices would probably reduce farm transfers temporarily and check the availability of farm mortgages.

Urban Real Estate Loans: - Expectations of consumers regarding the purchase of homes, as shown by this year's survey of consumer finances, indicate a smaller volume of transactions for residential properties than in 1946. On the other hand, a larger proportion of these purchases will be for new houses than characterized transactions last year. This will mean a reduced volume of repayment of outstanding mortgages resulting from property transfers, and a steady, though smaller, flow of new mortgages. As a result, urban mortgage loans may increase by nearly 1.8 billion dollars during the current year, and because of the large backlog of demand for housing, further expansion may be expected in the first half of 1948.

Consumer loans: - Consumer purchase expectations, as reported in the 1947 survey of consumer finances, indicate a continuing strong demand for automobiles and the purchase of all the cars that can be produced, as well as all of the used cars that become available. Growth in demand for other consumer durables, however, seems to be slackening. A special factor in consumer credit demand, because of the narrowed margin between income after taxes and expenditures and the prospects of some rise in unemployment, will be borrowing to meet family deficits and emergencies. Income tax relief may, of course, moderate such demand somewhat. A declining rate of collections on consumer credit outstandings during the months ahead will mean a longer average period of consumer indebtedness and will help to sustain expansion in consumer credit outstandings.

All in all, the outlook is for a steady rise in consumer credit outstandings of banks, amounting to perhaps 1 billion dollars this year and continuing at that annual rate during the first half of 1948. Total consumer credit is currently increasing at an annual rate of about 2.8 billions.

Loans for Purchasing and Carrying Securities: - Of all the loan categories, only security loans have the prospect of registering a decline. Sluggish and uncertain stock market conditions are expected to continue through the year, with the result that a decrease in security loans of about 1 billion dollars is not unlikely. Prospects for 1948 depend on the willingness of smart money to discount optimistically the business outlook at that time on margin requirement policy.

Total Loans: - Addition of bank loan prospects, as summarized above, yields a net increase for this year of 4 billion dollars and this projection appears to be on the conservative side. The possible advent of recession the latter half of 1947 makes loan tendencies for early 1948 uncertain, but the odds of over-all loan market prospects at this stage favor a small net increase in the first half of next year.

Bank Investments: - Debt retirement for the year, less replacements of retired securities as banks may make, is expected to reduce commercial bank holdings of Government securities by about 3 billion dollars. On the other hand, holdings of other securities will likely expand by at least 1 billion, so that net decline in commercial bank investments would amount to 2 billions. Some further moderate decline in bank holdings of U. S. Governments may be assumed as likely during the first half of 1948, but the prospect is for this decline to be more than offset by increased holdings in other securities.

Increased holdings of other securities will reflect bank purchases of about half of the offerings of State and municipal issues, which will be in record volume during this year, plus some bank purchases of issues by the International Bank and some further buying of corporate issues. Retirement of corporate bonds may about equal new issues during 1947; therefore, little change in the total supply of corporate securities having bank investment quality is to be anticipated.

Bank Reserves: - On the assumption of some recession in business starting in the near future, a less than seasonal increase in money in circulation is expected towards the end of 1947. For the year as a whole, in consequence, bank reserves will be augmented by perhaps half a billion dollars from a return of currency from circulation, most of which has already occurred. Foreign needs for dollar exchange will bring about a steady gold inflow, with the total for the year possibly amounting to 1 billion dollars. Because of continuing deposit expansion, individual banks will probably sell Government securities to the Reserve Banks from time to time to maintain reserve positions, but banks generally will be under no great pressure to obtain reserves through this mechanism. At this stage, further currency and gold inflow appears to be a reasonable expectation for the first half of 1948.

Deposits and Total Money Supply: - Deposit changes at commercial banks during this year will comprise: (a) a reduction of 2.2 billion dollars in war loan deposits carrying such deposits by the year-end to a level of about half a billion; (b) an increase of nearly 3.5 billions in adjusted demand deposits, and (c) an increase of 1 billion, or more, in time deposits. In addition, time deposits at mutual savings banks and postal savings will probably increase about 1 billion dollars.

Altogether the picture presented is one of moderate expansion in total money supply this year. A substantially larger expansion, however, is in prospect in the money supply held by the public. This increase will

amount to around 5 billion dollars, or about one-third of last year's expansion in the public's money supply. Tendencies likely to be encountered in the first half of 1948 may reduce this rate of increase; but some further monetary expansion seems possible in that period.

We thus confront the anomaly of prospective moderate business recession combined with further monetary expansion resulting from private credit expansion. Since economic recession may be accompanied by important downward price adjustment in certain sectors, this continuing bank credit and monetary expansion cannot be appropriately described as immediately inflationary. The resulting addition to the nation's money and liquid asset stocks, however, will be a source of inflationary pressures in the revival that will ensue in due course; in fact, the existence of larger money and liquid asset stocks may check recession and hasten and accelerate revival.

It is important to emphasize that the sources of prospective credit expansion are not demands especially responsive to moderate increases in short-term interest rates. Another point of emphasis is that the projected bank credit and monetary expansion is reasonably conservative. It assumes no general tendency for banks to expand holdings of Federal debt, and only a moderate increase of private debt and of municipal and State debt as a source of bank assets. Because of discontinued pressure on bank reserve positions from further debt retirement, tendencies in the direction of further bank credit expansion through bank shifting from short to longer-term Government securities may be stronger than expected. Another factor that might accelerate monetary expansion would be a more ample availability than now seems reasonable to anticipate of other types of bank assets.

Bank Earnings and Bank Capital: - Gross earnings of member banks in 1946 exceeded the previous high reached in 1945. Expenses, however, also rose to new high levels with the result that the average return after taxes on stockholders' investment declined somewhat from the 10.9 per cent attained in 1945. The average return in 1946 of 9.6 per cent was still the highest peacetime level for member banks since 1920.

Banking developments in prospect will likely lower further the level of bank profits on stockholders' investment in 1947. Gross bank earnings in 1947 will equal or exceed earnings in 1946 but expenses will be higher, recoveries and profits on securities will be lower, and losses and charge-offs will probably rise. On balance, the outlook is for a decline in the average return on stockholders' investment, perhaps to a level close to 8.5 per cent.

Banks have added substantially to capital through retained earnings since prewar days and bank capital is now higher than ever before. Recent bank loan expansion has reduced the ratio of capital to risk assets, which had attained the highest levels since 1914 during the war period; in fact, the ratio at the end of last year was below levels that prevailed

during most of the Thirties. During 1947, the decline will continue but will probably be arrested in 1948. This development suggests that a bank capital problem may be taking shape and that a growing number of banks will be confronted in the next period of business expansion with a need to strengthen their capital positions by the sale of additional stock.

### Treasury Finance, 1947-1948

Fiscal developments will likely continue to exert a moderately anti-inflationary influence, but the outlook for Treasury finance is still very uncertain. It can be said with certainty, nevertheless, that by mid-1947 the period of large-scale retirement of marketable debt will be over. The Treasury balance at the end of June will be in the neighborhood of 2.5 billion dollars, including 1 billion of gold, or close to a working minimum. Accordingly, any future debt retirement will have to be out of current budget surplus and from receipts from nonmarketable debt. Whatever the actual budget for the fiscal year 1947-1948 may turn out to be, reductions in the marketable debt during that year will hardly exceed 2.5 billion dollars (which total represents an estimated amount of voluntary redemptions if all maturing issues are refunded) as compared with about 21 billion dollars in the fiscal year just closing.

This means that the debt management problem henceforth will be one of refunding. Total maturities during the next fiscal year, not counting Treasury bills, will amount to 36.5 billion dollars. Of this nearly 7 billions will be in bonds, about 4.5 billions in notes, and just over 25 billions in certificates. The way in which the refunding is handled will be an important element in determining the pattern of market interest rates and the shift in the ownership distribution of security holdings.

Budget for the Fiscal Year 1946-1947: - Expenditures for the current fiscal year are estimated at 41.5 billion dollars and receipts at 42.5 billions. The resulting surplus of 1 billion, together with about 8 billions from receipts on nonmarketable securities (over 2 billions of which was in the form of securities issued to the International Fund and Bank) and a reduction in the General Fund balance of nearly 12 billions has permitted retirement of public marketable debt of around 21 billion dollars.

Budget Outlook for the Fiscal Year 1947-1948: - For 1947-1948, the President's budget recommendations provided for an expenditure level of 37.5 billion dollars. The House Committee on the Legislative Budget voted that this total be reduced to 31.5 billion dollars and the corresponding Senate Committee vote provided for a reduction to 33 billion dollars. It is entirely improbable, however, that expenditure reductions of anywhere near the size indicated will be enacted. As far as can be figured, reductions which have been voted on to date provide for a cut of little more than 1 billion dollars, and will be offset by the additional appropriation of 400 million dollars for aid to Greece and Turkey. The

maximum cut that might be expected is, say, 2.6 billion dollars which would include a cut in national defense expenditures of 1.6 billions. However, these cuts are uncertain. The President's budget for total expenditures may well be reached; indeed, it might be exceeded.

The estimate of receipts involves a double uncertainty: first, with respect to revenue legislation and second with respect to the level of income upon which tax receipts depend. It may be assumed that reductions in personal income tax rates will be enacted involving a revenue loss equal to 20 per cent of income tax yield and that this reduction will become effective July 1. Also, it may be assumed that the statutory increase in payroll tax rates, scheduled for January 1, 1948, will be again postponed.

If the projected moderate recession of business is realized, income payments may decline from an annual rate of about 170 billion dollars in the third quarter of this year to an annual rate of 152 billions in the first half of 1948. On this basis net receipts of the Federal Government may approximate 36.6 billion dollars. This is about 6 billion dollars below receipts for the current fiscal year.

With expenditures of about 35.3 billion dollars and net receipts of 36.6 billions we arrive at a budget surplus of 1.3 billion dollars for the coming fiscal year. Broken down by quarters this reflects deficits of three-quarters of a billion dollars each for the third and fourth quarters of this calendar year, a budget surplus of nearly 4 billions for the first quarter of next year, and a renewed deficit of slightly more than 1 billion for the second quarter of 1948.

Fiscal Developments and Debt Retirement: - For this calendar year as a whole, the fiscal outlook is for budget balance or a very slight budget deficit, the deficit for the second half of the calendar year of 1.5 billion dollars about offsetting the surplus for the first half. Income from non-marketable debt and reduction in Treasury balances will be the source of funds for this year's net retirement of public debt exceeding 8 billion dollars.

During the first half of 1948 there may be a surplus of receipts close to 3 billions. Retirement of another 2 or 3 billions of marketable debt might be possible from the expected budget surplus and a further increase in nonmarketable debt.

Our projection for changes in holdings of Federal debt by the banking system for the calendar year 1947 is a decline of about 5 billion dollars, distributed - 3 billions to commercial banks and 2 billions to Federal Reserve Banks. This implies a decline in holdings of marketable debt by nonbank investors during the year of more than 3 billions. Probably insurance companies and mutual savings banks will increase their holdings somewhat, while under the impact of full-employment followed by

recession readjustments, business corporations, and to some extent individuals, may decrease their holdings. In all likelihood, the pattern of change in holdings during the first half of 1948 will be similar but the size of the changes will be smaller because of a prospective low volume of retirements.

Potentialities of Sharper Recession: - A sharper recession than has been projected would have different fiscal repercussions than we have outlined. The budget surplus assumed for the fiscal year 1947-1948 would be converted into a deficit; marketable debt would increase rather than undergo any further decline; holdings of Government securities by commercial banks and Federal Reserve Banks would increase rather than decline; holdings by corporations and individuals would fall off more sharply than projected; and additional investment by insurance companies and savings banks might be larger than anticipated. In the event of more than moderate recession, furthermore, bank loans would probably be reduced, but this might well be more than offset by additional credit released from new bank financing of the Government's deficit. On balance, expansion in the money supply would probably be greater than this report has indicated.

\* \* \* \* \*

The foregoing projections of banking, monetary, and fiscal tendencies for the period ahead are set forth to indicate the general pattern of financial developments that might be expected on the showing of current information and the potentialities indicated by projections of national product and income. The projections are not to be considered as forecasts; there are many possibilities for different results to emerge. While they are based on assumptions that appear reasonable, it is important to keep in mind that the period ahead promises to be one of rapid economic change. Many unanticipated factors will undoubtedly influence the course of developments.

	1947	1948	1949	1950	1951
Reserve Assets and Liabilities	1.0	1.0	1.0	1.0	1.0
Government Securities	1.0	1.0	1.0	1.0	1.0
Commercial Bank Loans	1.0	1.0	1.0	1.0	1.0
Other Assets	1.0	1.0	1.0	1.0	1.0
Other Liabilities	1.0	1.0	1.0	1.0	1.0
Total	1.0	1.0	1.0	1.0	1.0

Table 1  
Factors Affecting Deposits and Currency  
(Billions of dollars)

	Dec. 1945	Dec. 1946	Dec. 1947*	Change during	
				1946	1947*
<b>Expansive Factors</b>					
<u>Commercial Banks</u>					
Loans - total . . . . .	26.1	31.1	35.1	+5.0	+4.0
Commercial . . . . .	9.5	14.0	15.8	+4.5	+1.8
Agricultural . . . . .	1.3	1.4	1.5	+0.1	+0.1
Real Estate . . . . .	4.7	7.1	9.0	+2.4	+1.9
Rural . . . . .	(0.5)	(0.7)	(0.8)	(+0.2)	(+0.1)
Urban . . . . .	(4.2)	(6.4)	(8.2)	(+2.2)	(+1.8)
Purchasing Securities . . . . .	6.8	3.1	2.1	-3.7	-1.0
Consumer . . . . .	2.4	3.7	4.7	+1.3	+1.0
Other . . . . .	1.4	1.8	2.0	+0.4	+0.2
Investments - total . . . . .	97.9	82.9	79.9	-15.0	-2.0
U. S. Government					
Securities . . . . .	90.6	74.8	71.8	-15.8	-3.0
Other Securities . . . . .	7.3	8.1	9.1	+0.8	+1.0
<u>Federal Reserve Banks</u>					
U. S. Government Securities	24.3	23.4	21.4	-0.9	-2.0
<u>Treasury</u>					
Treasury Currency . . . . .	4.4	4.6	4.7	+0.2	+0.1
Gold Stock . . . . .	20.1	20.5	21.5	+0.4	+1.0
<b>Contractive Factors</b>					
Treasury deposits at banks . . . . .	24.6	2.7	0.5	-21.9	-2.2
Treasury deposits at Reserve Banks . . . . .	1.0	0.4	0.2	-0.6	-0.2
Nonmember deposits and other Federal Reserve accounts . . . . .	1.8	1.4	1.5	-0.4	+0.1
Treasury Cash . . . . .	2.3	2.3	1.3	n.c.	-1.0
Net Bank Capital and Other . . . . .	10.6	11.4	11.9	+0.8	+0.5
<b>Deposits and Currency</b>					
<u>Deposits</u>					
Demand deposits, adjusted . . . . .	75.9	83.6	87.0	+7.7	+3.4
Time deposits (commercial banks) . . . . .	30.1	33.9	35.0	+3.8	+1.1
<u>Currency</u>					
Currency Outside Banks . . . . .	26.5	26.8	26.2	+0.3	-0.6
<b>Memorandum</b>					
Time Deposits at Mutual Savings Banks and Postal Savings . . . . .	18.3	20.1	21.1	+1.8	+1.0

PROJECTED TREASURY FINANCES  
(Provisional estimates. In billions of dollars<sup>1/</sup>)

	1946	1947			1948		Calendar	Fiscal Year	
	July Dec.*	Jan. June	July Sept.	Oct. Dec.	Jan. Mar.	Apr. June	year 1947	1947	1948
Treasury cash balance, start of period	14.0	3.1	2.5	1.9	1.7	5.7	3.1	14.0	2.5
Net receipts	18.5	24.0	8.8	7.7	12.1	8.0	40.5	42.5	36.6
Expenditures <sup>2/</sup>	18.9	22.6	9.6	8.4	8.2	9.1	40.6	41.5	35.3
Surplus or deficit	- .4	1.4	- .8	- .7	3.9	-1.1	- .1	1.0	1.3
Change in nonmarketable debt	2.7	3/45.8	1.0	- .1	1.1	1.5	6.7	8.5	1.5
Retirement of marketable debt <sup>4/</sup>	-13.0	- 8.1	- .8	1.6	**	**	- 8.3	-21.1	**
Net change in cash balance <sup>5/</sup>	10.9	- .6	- .6	- .2	4.0	- .6	- 1.4	11.5	
Treasury cash balance, end of period	3.1	2.5	1.9	7/1.7	6/5.7	6/5.1	7/1.7	2.5	

\* Actual

\*\*No estimate

- <sup>1/</sup> Estimates are based on certain assumptions with regard to expenditures, tax legislation, and debt retirement policies; (1) expenditures for fiscal 1948 are assumed reduced by 2.6 billion dollars from the President's Budget, (2) personal income tax rates are assumed reduced by 20 per cent beginning July 1, 1947.
- <sup>2/</sup> Including net expenditures in trust account.
- <sup>3/</sup> Including 1.8 billion dollars of securities held by the International Monetary Fund and 400 million by the International Bank.
- <sup>4/</sup> For the third quarter of 1947, the reduction in marketable debt is assumed to equal voluntary cash redemptions, notwithstanding full exchange offerings for maturing issues. For the fourth quarter of 1947 the increase allows for some new financing. No marketable debt figures are shown for 1948.
- <sup>5/</sup> The Treasury's budgetary surplus or deficit plus changes in debt may not necessarily add to changes in the cash balance due largely to estimated or actual differences in timing of receipts and expenditures.
- <sup>6/</sup> The balance for 1948 will be lower or higher, depending on changes in marketable debt.
- <sup>7/</sup> Consisting of 200 million dollars in deposits with the Federal Reserve Banks, 500 million in war loan deposits and 1.0 billion of free gold of which 832 million gold transferred to the cash balance as a result of payments to the International Monetary Fund.

On May 20, 1947, at 10:45 A.M., the Federal Advisory Council held a joint meeting with the Board of Governors of the Federal Reserve System in the Board Room of the Federal Reserve Building.

All members of the Council were present except Mr. Charles E. Spencer, Jr., for whom Mr. Walter S. Bucklin served as an alternate and Mr. W. Randolph Burgess for whom Mr. John C. Traphagen served as an alternate.

The following members of the Board of Governors were present: Chairman Eccles; Governors Szymczak, Draper, Evans and Clayton; also, Mr. Carpenter, Secretary of the Board of Governors. Mr. J. Leonard Townsend, Assistant General Counsel, participated in the discussion during the period when bank holding company legislation was being considered.

WHAT POLICIES SHOULD BE PURSUED BY AMERICAN COMMERCIAL BANKS IN MAKING OR PARTICIPATING IN LOANS ON FOREIGN-OWNED GOLD? IT IS BELIEVED THAT SUCH LOANS SHOULD NOT BE MADE IF THEY APPEAR TO BE SOUGHT FOR PREDOMINANTLY SPECULATIVE PURPOSES, AND THAT IN ANY CASE THEY SHOULD BE LIMITED TO AN INITIAL PERIOD OF 12 MONTHS, SUBJECT TO RENEWAL, IN ORDER TO PROVIDE OPPORTUNITY FOR PERIODIC REVIEW. WHAT ARE THE VIEWS OF THE COUNCIL?

E. E. Brown states the Council does not believe that American commercial banks should be restricted in making or participating in loans on foreign-owned gold, either in relation to the purposes for which the loans are made or the length of time for which the loans are extended. If the Federal Reserve banks have a right to make such loans, American commercial banks should have the right. The fact that foreign central banks do now show in their statements that the gold is pledged, is bad practice, but it is no worse for the American commercial banks to make loans under those conditions than for the Federal Reserve banks to make such loans. In addition, one criticism that has been made of such loans is that any country which borrows dollars on gold rather than selling the gold outright, places itself in a position to profit from an increase in the dollar price of gold. However, if we loan on gold, we give evidence of the fact that we do not believe gold will be devalued.

Eccles. Foreign central banks are not likely to borrow from private banks instead of the Federal Reserve banks unless the foreign central banks wish to speculate or obtain a long term loan. The Federal Reserve banks extend no credit longer than ninety days and they do not permit a continuation of the credit. Consequently, the foreign central banks go to private American banks, pay as high as 3 per cent interest, and borrow for as long as five years.

Eccles says that a policy committee, of which he and Szymczak are members, may recommend that the Treasury issue no license for a gold loan longer than 12 months or for renewals that would extend the loan longer than 12 months. In addition, this committee may recommend that if a loan appears to be predominantly for speculative purposes, no license should be issued. These recommendations apply to situations where gold is held in this country. Any loans which the Federal Reserve banks make are for short terms.

E. E. Brown asks whether the Federal Reserve banks ever renew the loans for successive periods so that they extend beyond a year.

Eccles replies he does not believe there have been any cases where the loans have been extended beyond a year, although in case of real need, the Federal Reserve banks would consider a special situation.

E. E. Brown mentions that at the end of World War 1, American commercial banks made a loan, secured by gold, to a Russian general who was fighting the Bolsheviks. This loan was made at the request of the State Department.

Eccles states that the Board does not wish the Treasury to issue licenses so that American commercial banks can make gold loans of a type which the Board would not wish the Federal Reserve banks to make. He does not believe there is any real conflict between the views of the Board and the Council.

IT IS REPORTED THAT SOME AMERICAN COMMERCIAL BANKS HAVE PARTICIPATED IN TRANSACTIONS IN GOLD AGAINST DOLLARS AT PREMIUM PRICES IN FOREIGN COUNTRIES. IT IS BELIEVED, FROM THE STANDPOINT OF NATIONAL POLICY, THAT SUCH TRANSACTIONS ARE UNDESIRABLE AND THAT AMERICAN COMMERCIAL BANKS SHOULD BE REQUESTED TO REFRAIN FROM ENGAGING IN THEM. DOES THE COUNCIL AGREE?

E. E. Brown says that the Council believes that such transactions in gold against dollars at premium prices in foreign countries may be undesirable. However, the Council believes that no action of the Federal Reserve banks to restrict these transactions should go further than a request to refrain from engaging in them. He comments that at the time of the Bretton Woods meeting, as Chairman Eccles will recall, some foreign governments wanted the United States to agree to police all kinds of exchange transactions, but the American delegates declined to agree. He mentions cases where American travellers in France exchange travellers' checks for francs in the black market. Frenchmen who get these travellers' checks are sometimes able to take them into countries where gold is obtainable or where they can retain the dollars. It is obviously impossible for American banks to police the action of all their customers. E. E. Brown thinks that if the Federal Reserve banks asked American commercial banks to refrain from engaging in these transactions, it would be adequate.

Eccles reports that the Board thought the Federal Reserve banks and the Treasury might issue a joint statement to the effect that gold is quoted in many markets in the world above the United States price. Dollars

are used illegally in some of these foreign countries to buy gold, and, as a result, these foreign countries are limited in their ability to buy our goods and services. As a matter of fact, some of these countries may even need to borrow more dollars from us. The Treasury and the Federal Reserve banks would request American commercial banks to refrain from using their facilities to make such transactions possible.

E. E. Brown states that the Council believes any action should be limited to a request.

IN VIEW OF THE CURRENT BUSINESS SITUATION, THE BOARD WOULD BE INTERESTED IN RECEIVING INFORMATION FROM THE COUNCIL AS TO WHETHER BANKS GENERALLY EXPECT A CONTINUING STRONG DEMAND FOR BUSINESS LOANS, FOR LOANS SECURED BY REAL ESTATE, AND FOR CONSUMER CREDIT; WHAT EFFECTS THE INVENTORY AND PRICE SITUATION ARE HAVING UPON THE LOAN POSITIONS AND POLICIES OF BANKS; AND WHETHER, IN THE VARIOUS DISTRICTS, THERE HAS BEEN ANY GENERAL TENDENCY FOR BANKS TO FOLLOW MORE RESTRICTIVE LOAN POLICIES, FOR LOAN RATES TO RISE, OR FOR BORROWERS TO REQUEST RENEWALS OF LOANS MORE FREQUENTLY. IN ADDITION, THE BOARD WOULD BE GLAD TO HAVE ANY GENERAL VIEWS WHICH THE COUNCIL MIGHT WISH TO EXPRESS.

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E. E. Brown states that the Council believes it best to state its conclusions regarding this item on the agenda in connection with the specific questions which have been raised as follows:

- (A) Do banks expect a continuing strong demand for business loans?
  - (a) The majority of the members of the Council expect a continuing good demand for business loans, but there were three members who reported some leveling off in the demand. Those who are extending term credits expect a continuing strong demand. Some large companies that expected to finance their expansion by stocks are unwilling to do it in the present markets and may use bank credit, including term loans.
- (B) Do banks expect a continuing strong demand for loans secured by real estate?
  - (b) A continuing strong demand for real estate loans is anticipated, but owing to the excessive cost of new construction a lessened demand is expected for loans for new buildings. Some of the districts report little increase in the number of real estate loans going into banks because banks believe the costs are too high. Many of these loans are going into insurance companies.

- (C) Do banks expect a continuing strong demand for consumer credit?
- (c) All banks making such loans, as well as banks extending credit to finance companies, are experiencing a strong and increasing demand.
- (D) What effects are the inventory and price situations having upon the loan positions and policies of banks?
- (d) In general, the members of the Council report a more cautious approach to lending policies. There are some lines of business in which frozen situations appear to be developing. Borrowers are requesting renewals of loans more frequently because of large receivables and inventories. The newer crop of bank officers see frozen situations developing and there is a possibility that these younger men may not only be cautious but too restrictive in their loan policies.
- (E) Is there any tendency for loan rates to rise or for borrowers to request renewals of loans more frequently?
- (e) There has been no tendency for rates on national names of the highest credit to rise above the 1-1/2 per cent rate which has prevailed, but rates for loans to smaller concerns and credits not of the highest grade have tended to rise somewhat. Rates on term loans in the last year have perhaps increased about 1/4 of 1 per cent. Some banks that loaned at 1-1/4 per cent have gone to 1-1/2 per cent, and some small banks have raised rates in some cases as much as one or two per cent. In Mr. Young's talk yesterday, he seemed to feel that commercial loans would not go into the banks in such great volume in the period ahead, but the amount of real estate loans going into banks might be rather large. The Council informed Mr. Young that some bankers, on the other hand, are inclined to believe that the situation will be reversed and that the real estate loans going into banks may not be so large as he indicated, but that the amount of commercial loans may be larger. Mr. Young stated that he would settle for a development of that kind.

WOULD IT BE ADVISABLE TO REDUCE THE PRESENT MARGIN REQUIREMENTS ON SECURITY LOANS?

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E. E. Brown states that this item was not on the agenda originally submitted to the Board for this meeting. The Council believes that a reduction in margin requirements is desirable at this time. The stock market is in a deflationary phase. It is very thin and price fluctuations are wide. There is in the opinion of the Council no danger that a reduction in margins would have any dangerous inflationary effect, or cause any considerable demand for credit, but it would operate to lessen wide fluctuations in stock prices. The Council would not favor a reduction in required margins below 50 per cent, but it believes the present 75 per cent requirement is too high. Brown adds that the Council realizes it is difficult to select the right time to change margin requirements, but that this difficulty is one of the problems the Board necessarily takes on when it has control of margin requirements.

Eccles. The Board has discussed this subject from time to time. The stock brokers are constantly agitating it. The Board feels the present situation does not warrant a reduction in margin requirements. There are still too many inflationary elements in the situation, such as the high cost of living. As a result of taking off all the controls last year, many maladjustments have developed in our economy. We have had more inflation during the last year than we have had in the previous five years. The more inflation we have, the more that will have to be liquidated. The stock market now reflects what is looked upon as an inevitable future adjustment in our economy. Profits cannot be kept up, and the wage level is more frozen than ever before. Companies that fail to set aside a part of their profits to take losses on their inventories may become poor credit risks. People of small means are cashing their savings bonds in denominations of \$25 to \$100, whereas people of larger means are not cashing them. Stock market credit is only an incident in the whole picture. The psychology of reducing margins now would be wrong. The public might feel the Board of Governors was trying to support the inflation, or the public might feel that the Board considered stock prices were low enough now. Very little credit would probably be used. However, anything that adds to the total credit is bad. Some downward adjustment would be desirable. It is not the time now, either, to reduce taxes. The Board has discussed the question of whether margins on bank lending should be removed. The Board felt the margin on bank loans was desirable to make effective the margin on brokers' loans. The time to change margin requirements is when there is a more substantial deflationary trend.

Fleming remarks that the market has been going down for some time and it is thin.

Eccles believes the thinness of the market has nothing to do with margin requirements. The thinness of the market is based on the demand and supply factors in relation to the economic situation.

Fleming states that a number of those interested in securities are waiting until the market settles. He recognizes that no time is a good time to change margin requirements, but he would dislike to see any hysteria develop because of a constantly declining market.

Eccles. There is practically no credit in the market to liquidate. The corrections necessary in our economy will come with insolvencies and unemployment. The farmers have become accustomed to living in clover, and they will have to live in less clover.

E. E. Brown. The government purchases for relief may be desirable in the interest of world economic recovery, but these purchases are a major factor in the high cost of living.

Eccles thinks the time for reducing margins may come somewhat later.

Bucklin believes it is a matter of the level of the margins. A 50 per cent margin is still a high margin.

Szymczak asks whether the market needs any credit at all. When the margin requirements were reduced to 75 per cent, very little credit entered the market and even that soon left the market. (Townsend enters the meeting.)

AT THE LAST MEETING IT WAS UNDERSTOOD THAT THE COUNCIL WOULD GIVE FURTHER CONSIDERATION TO THE HOLDING COMPANY BILL S. 829 AND THAT AT THE NEXT MEETING IT WOULD SUBMIT ITS VIEWS WITH RESPECT TO THE PROPOSED LEGISLATION.

E. E. Brown states that the Council is now in unanimous agreement on its recommendations regarding bank holding company legislation. There were sixteen members on the Committee of the Association of Reserve City Bankers which prepared the report on bank holding company legislation which was approved at the recent meeting at Swampscott. Of the sixteen members of the Committee, five are present members of the Council and six are former members. Brown understands that all the holding companies but Transamerica have agreed to the principles formulated at Swampscott. He also understands that the American Bankers Association will not take any part in discussing the problem. However, for the first time there is wide agreement among bankers on the principles. Brown says the council is familiar with the holding company bill introduced in the Senate, S. 829. It understands this bill is shortly to be rewritten, and that the rewritten bill to be substituted for Senate bill 829 will follow the general lines of that bill. Obviously, the Council can not approve a bill which it has not yet seen and which has not been introduced. However, (1) it believes that holding company legislation is desirable at this time; (2) it approves the general approach to the holding company problem embodied in Senate bill 829; and (3) it believes that the new bill should contain:

(a) A more definite statement of the objectives of the bill and of standards for Federal Reserve Board action. The incorporation in the bill of objectives and standards along the lines suggested in the recent report of a Committee of the Association of Reserve City Bankers would meet the Council's approval. The three essential goals of the legislation as formulated and approved at the Swampscott meeting are:

1. to reach and regulate any banking operation which, functioning in an area or with a structure larger than that permitted to independent banks, can or does, through the medium of concentrated control, jeopardize independent competitive banking at local or regional levels or place independent banks under the particular circumstances at a competitive disadvantage;
2. to confine the size and geographical extent of any such banking operation, regardless of its competitive or other aspects, within limits consistent with adequate and sound banking; and
3. to control the magnitude and geographical extent of any such banking operation, regardless of all other considerations, to the end that, in the event of adverse general economic conditions, such an operation will not be subjected to an inordinate pressure arising from unwieldiness due solely to mere size and expanse which, in turn, may put an inordinate pressure on the nation's banking structure.

(b) Simple justice requires that if holding companies are required to divest themselves of non-banking assets, they should be granted tax exemption in connection with such divestment. A precedent exists for this in the utility holding company legislation.

(c) A larger percentage of ownership of stock in two or more banks than 10 per cent should be required to automatically create a holding company relationship. Brown mentions that this point is not suggested by the holding companies, but is suggested by those bankers who do not wish to be considered part of a holding company group because ten per cent or more of their stock is held by some owner such as an insurance company which may own ten per cent of the stock of two or more banks.

(d) There should be provisions that incidental ownership of bank stocks in fiduciary capacities such as executor,

trustee under a will, etc., should not create a holding company relationship.

E. E. Brown points out that there is more widespread agreement on the legislation than ever before. He has talked with Wiggins and he believes the Treasury might go along with the legislation. However, he does not know the viewpoint of the Federal Deposit Insurance Corporation.

Eccles states that the powers of the Board have not been adequate to control the holding company situation. Independent West Coast bankers have strongly urged legislation. The Board would not introduce a bill that did not have widespread support.

E. E. Brown states that Odlin reports the West Coast independent bankers would go along with legislation along the lines Brown has outlined. He understands Senate bill 829 may not be rewritten but may be amended.

Eccles reports that the Board does not propose to introduce another bill. An earlier bill was found to apply to many situations in which the Board had no interest. The present bill is actually the third bill and Eccles does not wish to introduce a new bill as Congress may think the Board did not know what it was all about in the previous bills. He wishes to keep as much as possible of the present bill.

E. E. Brown thinks many bankers will insist on the points he has outlined as the Council's viewpoint.

Townsend states, in response to Eccles' request for his comment on the proposal contained in paragraph (a) of the Council's statement, that it is felt that, if authority is given to the Board to regulate the expansion of bank holding companies, that authority should (1) parallel as closely as possible the procedures that had been traditional in the banking statutes, that is, the filing of an application and consideration by the Board of the matters which under the present law must be considered by the Comptroller of the Currency and the Board in connection with the approval of the establishment of branches by banks, and (2) require, in addition, consideration of the prohibitions against restraint of trade and monopoly that had been in Federal statutes and which would confine bank holding companies within the existing prohibitions of law as applied in the field of commerce and industry. He says that the first point was covered by the first part of paragraph 6(d) of the existing bill, which was taken from existing statutes, and which required that consideration be given to the financial history and condition of the applicant and the banks concerned, their prospects, the character of their management, and the convenience, needs and welfare of the communities and the area concerned, and that the second point was covered by the part of the paragraph which required consideration of the national policies against restraint of trade and undue concentration of economic power and in favor of the maintenance of competition in the field of banking. With respect to the standards included in the report of the Reserve City Bankers' Association, Townsend feels that

it could be demonstrated that all of these standards were included within the scope of paragraph 6(d) as contained in the present bill and would be a part of the Board's thinking in considering any acquisition covered by the section, and that, therefore, the problem is a question of the choice of language.

E. E. Brown remarks that the holding companies believe the Swampscott proposals would restrict holding company operations more than the language of the present bill. However, the holding companies have agreed to the Swampscott proposals although they opposed them for some time.

Townsend. The bill requires the Board to consider each individual situation and to determine whether monopoly is being promoted or whether competition is being stimulated. With respect to tax exemption, the Board favors it, but the Treasury will have to pass upon it. The Board might then pass along to Congress the viewpoint of the Treasury. With respect to the figure of 10 per cent, it has long been unnecessary to own a majority of the stock to control a bank. A company which owns 10 per cent or more of the stocks of two or more banks may maintain it is not a holding company. It only needs to write a letter requesting exemption which can be granted unless, in fact, the company actually is a holding company. Some companies control on the basis of 10 per cent or less, and in some instances there is actual control without the ownership of any stock. The Reserve City Bankers gave no reason for wanting 20 per cent, but merely stated they would like it as a more convenient figure. The 10 per cent is one of the essential musts of the bill.

E. E. Brown. The Council recognizes that the Board can bring in an owner of bank stocks, and the burden is on the party brought in to prove that he should be called exempt. It is entirely a question of the size of the net. The Council believes there are too many situations where banks would be caught in a 10 per cent net, and the banks do not wish to go through the trouble of proving that they should be exempt. The bigger the size of the holes in the net, the smaller the number that will be brought in under the proposed legislation. The holding companies know they are brought in under the legislation, and they are not so concerned about this figure. It is the independent banks who want a figure higher than 10 per cent, as they do not wish to be brought in under the legislation.

Townsend. Any legislation that leaves out banks that should be brought in is not good legislation.

E. E. Brown. It is not a question of leaving anyone out, as the Board could still bring in anyone.

Eccles. Any owner knows whether he is controlling a bank. An insurance company could state, perhaps by a formal statement of its board of directors, that it was not controlling a bank.

Odlin. The West Coast independent bankers have no objection to the 10 per cent but other bankers have.

E. E. Brown. Many banks over the country do not wish to be subject to a dragnet unnecessarily. Holding companies do not object, but independent banks think they should not, under any condition, be included. They do not wish to be dragged in as a result of a figure as low as 10 per cent. In some cases, finance companies have taken over banks as feeders for their business. This development should be prohibited, and this is not covered by the present legislation. However, Brown believes it would be by the Swampscott proposals.

Townsend thinks the senators in the holding company states would oppose the insertion of the phrase, "geographical extent", expressed in points two and three of the essential goals of the legislation as stated in the Swampscott proposals.

E. E. Brown replies that the holding companies in those states have agreed to the goals as stated in the Swampscott proposals.

Eccles suggests that Townsend consider amending the bill to include the Swampscott proposals as they may be more clearly stated than the language used in the bill.

Townsend. The Board would have to analyze each case from the point of view of convenience, needs and soundness.

E. E. Brown. The company expanding might be held to be sound even though the expansion should not take place.

Eccles states he will discuss the bill further with Townsend. He suggests using the language of the bill, but supplementing it with the Swampscott proposals.

Odlin comments that he would dislike to see the bill bog down because of semantics. He thinks the bill would not be injured by rewriting it to include the Swampscott objectives. He also thinks changing from 10 per cent to 20 per cent is not an insurmountable point. He would prefer 10 per cent but perhaps an agreement could be reached on 15 per cent.

Eccles says that he argued for 10 per cent and Townsend had favored 15 per cent. Any company owning 10 per cent is probably controlling, but it might be difficult for us to prove it. As a practical matter 10 per cent constitutes control.

E. E. Brown states that holding company legislation is desirable from the public standpoint.

Szymczak thinks that the Board and the Council are in agreement on all of the Council's recommendations except the question of the 10 per cent or 20 per cent.

The Council reconvened in the Board Room of the Federal Reserve Building at 2:45 P.M. on May 20, 1947.

All members of the Council were present except Mr. Charles E. Spencer, Jr., for whom Mr. Walter S. Bucklin served as an alternate, and Mr. W. Randolph Burgess for whom Mr. John C. Traphagen served as an alternate.

BANK HOLDING COMPANY LEGISLATION.

E. E. Brown asks whether the Council wishes to give the Board of Governors a resolution on the holding company legislation as Eccles has suggested.

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After discussing the matter, the Council approved the resolution and memorandum which follow, together with the letter of transmittal from President Brown.

May 20, 1947

Honorable Marriner S. Eccles,  
Chairman,  
Board of Governors,  
Federal Reserve System,  
Washington 25, D. C.

Dear Chairman Eccles:

Transmitted herewith is resolution of the Federal Advisory Council passed at its meeting today.

Very truly yours,

(Signed) Edward E. Brown

Edward E. Brown, President,  
Federal Advisory Council.

Enclosures

FEDERAL ADVISORY COUNCIL

R E S O L U T I O N

The Council for the past few years has at almost every meeting discussed the holding company situation, the inadequacies of existing legislation, and proposals for additional legislation in connection with it.

(1) The Council believes that holding company legislation should be enacted at this time. Experience has shown that the present legislation is inadequate and that additional legislation is urgently necessary.

(2) It approves the general approach to the holding company problem embodied in Senate Bill 829.

(3) It believes Senate Bill 829 should be amended -

(a) By adding to the declaration of policy and the standards for Federal Reserve Board, Comptroller of the Currency, and Federal Deposit Insurance Corporation action a more definite statement of objectives and standards. (A memorandum is attached which was the subject of discussion between the Board of Governors and the Federal Advisory Council which indicates the type of amendments in this regard which the Council believes necessary.)

(b) By granting tax exemption to such holding companies as are required to divest themselves of non-banking assets. Simple justice requires that such tax exemption should be granted, and a precedent exists for it in the utility holding company legislation.

(c) By requiring a larger percentage than 10 per cent of the ownership of stock in two or more banks in order to create an automatic holding company relationship.

(d) By providing that incidental ownership of bank stocks in fiduciary capacities such as executor, trustee under a will, etc., should not create an automatic holding company relationship.

The Council urges the Board to submit amendments in accordance with these suggestions and to press for the enactment of the bill as so amended.

May 20, 1947

MEMORANDUM

1. To reach and regulate any banking operation which, functioning in an area or with a structure larger than that permitted to independent banks, can or does, through the medium of concentrated control, jeopardize independent competitive banking at local or regional levels or place independent banks under the particular circumstances at a competitive disadvantage;
2. To confine the size and expanse of any such banking operation, regardless of its competitive or other aspects, within limits consistent with adequate and sound banking; and
3. To control the magnitude and expanse of any such banking operation, regardless of all other considerations, to the end that, in the event of adverse general economic conditions, such an operation will not be subjected to an inordinate pressure arising from unwieldiness due solely to mere size and expanse which, in turn, may put an inordinate pressure on the nation's banking structure.

Association of Reserve City Bankers

Report on Bank Holding Company Legislation

Introductory Comments

At a meeting in Chicago last September, your Committee decided to inquire into the 'Bank Holding Company' situation. In the course of its inquiry your Committee has made it clear that it was merely exploring this matter on behalf of the Association with the ultimate aim of reporting its findings and conclusions to the Association so that the membership might be currently advised and thus be able to form a considered opinion on the subject. Furthermore, your Committee has not undertaken to promote legislation, to propagandize any particular type of legislation or to edit any proposed legislation.

Without going into detail, it may be fairly said that this report is an objective analysis of the composite thinking of many men active in the 'Holding Company' field, of many bankers not immediately connected with 'Holding Company' operations and of many individual unit bankers operating in the same field as 'Holding Companies'.

Underlying Issues

At the threshold we face two underlying issues of national policy, the answers to which control to a great degree anyone's initial thinking on 'holding company' legislation. These issues (assumed by many as settled, but questioned by not a few as lacking affirmative determination) are (1) are bank holding company operations, either within or beyond the state limits, to be prohibited or unrestricted or permissive under regulatory controls and (2) is branch banking by national banks to remain subject to the pleasure of the respective states and confined, where permitted, within geographical limits prescribed in the respective state laws?

Any early common agreement on these issues, a prerequisite to unanimity of thinking in respect of bank holding company legislation, is not to be expected. These issues persist from the historical controversy between unit banking, on the one hand, and holding company, branch and chain banking, on the other hand - spiced with all the traditions of the dual-banking system. There has been no federal affirmative legislation resolving in any final sense these questions of national policy.

It should be noted that bank holding companies grew up entirely without benefit of either national or state banking legislation and, relying on the general corporation laws of the respective states, moved into banking operations denied to both national and state banks. The Banking Acts of 1933 and 1935 gave them a legal status under federal law - predicated on regulatory controls. There is a broad sentiment that such controls have proved inadequate. The question, what to do in respect of bank holding companies, has again come to a head.

It should also be noted that the national banking system, starting as a 'unit banking' system, has progressed to a hybrid 'unit and branch banking' system, primarily through the negative process of placing national banks on a parity with state banks in states where branch banking is permitted. This also falls far short of any affirmative final determination of national policy in respect of branch banking by national banks in non-permissive states or across state lines on some regional basis or even on a national basis. This issue will acquire great importance if holding companies, encouraged possibly by a continuing gap in federal or state legislation, should in appreciable degree acquire banks within any particular state or region in which branch banking is not permitted to independent national banks and state banks. On the other hand, to the extent that any bank holding company legislation levels off inequalities, to a like extent does this issue of branch banking become less urgent.

The banking fraternity has not, in spite of much discussion, come to grips with these two issues. The American Bankers Association, however, in its so-called Boston Resolution, passed in 1937, pronounced itself as opposed in principle to banking beyond state lines, either directly or indirectly. The scope of the Boston Resolution, and its import so far as Association policy in respect of 'holding company' legislation is concerned, is presently under review by the Association.

In connection with 'holding company' operations in states where branch banking is permitted, another related underlying question crops up, to-wit, to what extent can branch banking by a national bank within such a state be restricted. Present federal legislation provides merely that such a national bank "with the approval of the Comptroller of the Currency" may establish and operate branches within the prescriptions of the state law and a state non-member insured bank shall not establish such branches "unless it shall have the prior written consent of the Federal Deposit Insurance Corporation". This issue would, it seems, resolve itself, at least temporarily, in the light of principles reflected in any 'holding company' legislation.

The above issues are recited primarily to indicate the divergence of viewpoints underlying the approach to bank holding company legislation. Quite obviously, a discussion of these issues is not timely and falls beyond the scope of this report. It would seem more useful and advisable, acting on the present status of federal and state legislation in the light of conflict in banking thinking on this subject, to adopt certain assumptions in respect of these issues and to proceed on these assumptions to a consideration of sound 'holding company' legislation. Any other course invites indefinite delay and a consequent continuing void in the control of the scope and practices of bank holding companies which potentially, in turn, can prejudice the position of independent banking and aggravate the issue of branch banking by national and state banks - not only in states where branch banking is not now permitted but also even beyond statelines. It is, of course, quite conceivable that state banks may ultimately,

through reciprocal state legislation, engage in branch banking even beyond state lines. In fact, such would seem to be an inevitable companion development in the event national banks should as a matter of national banking policy be allowed to operate branches beyond state lines.

In the following discussion of bank holding company legislation, therefore, we, as apparently have a preponderance of those with whom we have talked, assume that national policy is currently fixed as follows: (1) bank holding company operations, either within or beyond state limits, should be permissive under regulatory controls, (2) branch banking by national banks should not extend beyond the geographical limits prescribed in the laws of such respective states as permit branch banking, and (3) any extension of branch banking by national banks, within the limits prescribed in the respective state laws, should remain without change, i.e., subject to "the approval of the Comptroller of the Currency".

After all, unless the time is ripe to abandon the traditional concept that American banking is to be competitive between independent banks operating as units or with branches within state limits where permitted, there is not much violence in these assumptions. To be sure, the recognition of this concept in connection with bank holding company legislation will, at least inferentially, reaffirm it at this time without a review on the merits whether it is not too restrictive in the light of our present national economy. It seems more practical, nevertheless, to go forward with legislation which will bring bank holding company operations down more nearly on a par with current independent bank operations and leave the extension of branch banking by national and state banks to the future.

#### Committee Findings

Without inferring unanimity, it may be said confidently that there is a substantial preponderance of common thinking in respect of bank holding company legislation, as follows:

1. It is advisable to move forward with bank holding company legislation at this time.
2. Any such legislation, generally speaking, should contain a minimum of discretionary power in the enforcing agency.
3. The enforcement of the law may logically be lodged in the Board of Governors of the Federal Reserve System.
4. There should not be any so-called "death sentence" provision.
5. There should not be any blanket "freeze" provision.
6. The creation of new or the extension of existing 'holding companies' should be permissive, but the granting or withholding of permission should, so far as practicable, hinge on definite statutory norms - any adverse action of the enforcing agency to be reviewable in the courts.

7. Bank holding companies should be limited to the business of banking and other activities generally accepted as incidental to the banking business.

8. Existing 'holding companies' should be protected against undue sacrifice or harsh consequences in respect of any divorcement of their presently held non-banking assets or interests. In other words, such divorcement should not be forced under conditions precluding a disposition at fair value and should be accorded appropriate tax relief.

9. As to 'coverage', i.e., the type of operations to be encompassed by the legislation in the light of its objectives, it is evident that a coverage, sufficiently inclusive and exclusive at the same time, cannot be arrived at exclusively on an 'automatic' basis, i.e., by legislative definition or formula alone, and requires also resort, in greater or less degree, to 'administrative' determination, i.e., quasi-judicial powers in the enforcing agency.

10. The 'automatic' coverage should not be in the nature of a drag-net - but should be related to the objectives of the legislation.

11. Percentages of deposits or banking offices in a particular area are not satisfactory norms of 'automatic' coverage.

12. The objectives of the legislation should be precisely stated and those objectives should become the statutory norms controlling the exercise of discretionary power lodged in the enforcing agency.

13. The mechanical requirements of the legislation do not offer any questions of serious or unsurmountable nature.

#### Committee Comments

The obvious problem is how to reduce the concepts, listed above, to a workable piece of legislation - more particularly, how to avoid an excess of indefinite discretionary power in the enforcing agency and yet provide a mechanism which will with certainty encompass such operations and only such operations as lie within the intended scope of the legislation. This query pertains primarily to the question of initial coverage but also, of course, bears on other discretionary powers, such as the creation of new or the extension of existing 'holding companies' and the application of controls by the enforcing agency under the law. The only answer seems to lie in a legislative specification of the law's objectives - expressed not in abstract or abstruse generalizations but as far as possible in understandably precise statements. The starting point of any attempt at such a specification is, obviously, a determination of the goals of the legislation.

Essential goals of the legislation should, it seems, be

1. to reach and regulate any banking operation which, functioning in an area or with a structure larger than that permitted to independent banks, can or does, through the medium of concentrated control, jeopardize independent competitive banking at local or regional levels or place independent banks under the particular circumstances at a competitive disadvantage;
2. to confine the size and geographical extent of any such banking operation, regardless of its competitive or other aspects, within limits consistent with adequate and sound banking; and
3. to control the magnitude and geographical extent of any such banking operation, regardless of all other considerations, to the end that, in the event of adverse general economic conditions, such an operation will not be subjected to an inordinate pressure arising from unwieldiness due solely to mere size and expanse which, in turn, may put an inordinate pressure on the nation's banking structure.

If, among possible others, these be the goals and they be expressly adopted as the 'objectives' of the legislation, they would seem to provide reasonably precise statutory norms, for the exercise of discretionary powers delegated to the enforcing agency. Moreover, they would seem to provide norms under which the enforcing agency could properly be granted discretionary power to relieve any 'holding company' from the requirements and controls of the law to the extent that their application is unneeded in the light of the nature and degree of the conflict with the respective objectives of the law.

Finally, a word as to 'coverage'. The legislation should be designed as far as possible to reach only operations which, through the medium of the exercise of concentrated control, come into conflict with one or more of the objectives of the legislation. The intangibles in this equation are, first, what is control and, secondly, under what circumstances is the exercise of such control to be presumed or to be proved as existing in fact. Obviously, mere ownership without actual exercise of control is less likely to create situations leading to conflict with the objectives of the law than is an actual exercise of control with a slight degree of or even without ownership. An initial coverage, sufficiently exclusive and inclusive, appears to require a combination of an 'automatic' and an 'administrative' coverage.

The 'automatic' coverage would rest on a legislative formula providing that a specified percentage of stock ownership in each of two or more banks, directly or indirectly, would constitute a holding company operation. Just what this percentage of stock ownership should be has

been a subject of much discussion. If too low a percentage is adopted it will initially tag as 'holding companies' innumerable incidental stock holdings in two or more banks by individuals, corporations, and trustees, which are totally unrelated to any 'holding company' operation. Moreover, it seems unrealistic to fix a low percentage by way of a drag-net and then provide that such percentage of ownership in two or more banks makes it a 'holding company' unless the enforcing agency declares, at its own pleasure, that it is not a 'holding company'. From discussions on this subject during our exploration, the preponderant thought seems to be that, for the purpose of the 'automatic' coverage, the percentage of stock ownership should be fixed at, say, twenty per cent in two or more banks - on the theory that twenty percent ownership as a practical matter may be deemed to reflect or at least approach a dominant ownership and also that it reflects the minimum of ownership sought by anyone who intends in fact to exercise control. Twenty per cent ownership seems also to be a happy breaking point between the 'automatic' coverage and the 'administrative' coverage. If a particular 'automatic holding company' does not conflict with the objectives of the law, it could be declared by the enforcing agency to be an 'exempt' holding company and, as such, be automatically, by statutory provision, relieved from the requirements and controls of the law - subject to revocation of its 'exempt' status for cause. To eliminate temporary technical violations, the enforcing agency could by general order anticipatorily 'exempt' any future incidental 'automatic holding company', subject to later determination whether its operations are in conflict with the objectives of the law.

The 'administrative' coverage would authorize the enforcing agency, under a quasi-judicial power, to declare on the basis of evidence produced before it that a particular operation, whatsoever the degree of ownership, is a 'holding company' operation in that there exists in fact a concentrated control of two or more banks and comes in conflict with the objectives of the law--any such declaration to be reviewable in the courts and to be sustained if supported by substantial evidence.

It would seem that this dual 'automatic' and 'administrative' coverage should encompass with certainty any 'holding company' operation worthy of the name.

In conclusion, we repeat that this report primarily is merely our appraisal and analysis of various viewpoints expressed to us during the course of our exploration plus an attempt to reduce them to an acceptable common denominator. We started with no preconceived notions and finish with no unalterable personal convictions. If our discussions with others and this report tend to focus the thinking on the subject or

to reconcile in some degree conflicting viewpoints, they will have served a useful purpose.

Respectfully submitted,

William F. Kurtz, Chairman  
Harold V. Amberg  
Julian B. Baird  
Daniel W. Bell  
Keehn W. Berry  
Edward E. Brown  
W. R. Burgess  
Guy Emerson  
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Robert V. Fleming  
Robert M. Hanes  
James M. Kemper  
W. A. Mitchell  
Charles E. Spencer, Jr.  
G. W. Wallace  
H. Lane Young

Approved by the Association,  
May 14, 1947.

Committee on Federal Relationships -  
Association of Reserve City Bankers.

Memorandum to the Members of the  
Federal Advisory Council:

May 22, 1947

Leonard Townsend called me up yesterday, May 21, and said:

1. That the Board was willing to make the test of an automatic holding company relationship 15% of stock ownership in two or more banks instead of 10%.
2. That as to objectives, the Board, after a good deal of discussion, was willing to add to sub-section (d) of Sec. 6 of the Bill a clause reading as follows:

"provided, however, that nothing herein contained shall be construed to authorize the approval of any acquisition subject to paragraphs A, B or C of this section where, regardless of its competitive or other aspects, the effect of such acquisition may be to expand the size and extent of a bank holding company system beyond limits consistent with adequate and sound banking."

and asked my opinion as to whether this would be satisfactory. I asked and obtained his permission to discuss the Section with Harold Amberg, who had been active on the Reserve City committee, and also with Julian Baird and Cameron Thomson, to see whether it would meet their views.

Personally, I would be satisfied with the addition of this Section as meeting the suggestions contained in the Council's resolution. Harold Amberg thought it would satisfy the spirit of the Reserve City report, and both Thomson and Baird, after consulting their lawyers, said that while they did not care for it they were willing to take it for their companies and to recommend its acceptance to the other companies with whom they had been associated.

I called Townsend back today and stated that the proposed amendment was satisfactory to me personally but that I of course could not commit the other members of the Federal Advisory Council although I hoped they would also regard it as satisfactory, that Harold Amberg had stated it was satisfactory to him as one of the authors of the report of the Committee on Federal Relationships of the Association of Reserve City Bankers and that he believed it would be satisfactory to the majority if not all of the committee, but that he could not commit them, and that it was satisfactory to the First Bank Stock and the Northwest Bancorporation, but that Mr. Thomson and Mr. Baird had made it clear that while they would recommend its acceptance to the other holding companies they could not bind them.

This is for your information and until some definite action is taken by the Federal Reserve Board, please regard it as confidential.

E. E. Brown

AMENDMENTS TO S. 829 WHICH ARE RECOMMENDED  
BY THE BOARD

Amend Section 3 as follows:

Change the figure "10" appearing on page 2, line 20, to the figure "15".

Insert the following after the comma on page 2, line 21:

"or any company which is a bank and which directly or indirectly owns, controls, or holds with power to vote 15 per centum or more of the voting shares of one or more other banks,"

Change the figure "10" appearing on page 4, line 8, to the figure "15".

Add new subsection (f) as follows:

"(f) For the purposes of this section there shall be excluded from consideration all voting shares of banks or other companies acquired or held by a bank in a fiduciary capacity, except where such voting shares are acquired or held for the benefit of all or a majority of the persons beneficially interested in such bank or except where the Board, after notice and opportunity for hearing, finds that such acquisition or holding is being employed as a device for avoiding the provisions of this Act."

Amend Section 5 as follows:

Add the words "banking or" on page 7, at the end of line 4.

Add the following after the comma on page 7, line 14:

"or engage in the business of furnishing managerial, auditing, supervisory, purchasing and other similar services solely to such bank holding company and its subsidiaries, or in the business of procuring and servicing solely for such bank holding company and its subsidiaries investments and paper eligible for bank investment, or in the business of liquidating assets acquired from such bank holding company and its subsidiaries,"

After the word "subsidiaries" and before the semicolon on page 7, line 22, add the following: "or with the prior approval of the Board".

Add new subsection (d) as follows:

"(d) Nor shall the prohibitions of this section apply to voting shares or other securities or obligations which are held or acquired by a bank in a fiduciary capacity or which are otherwise lawfully owned by such bank on the effective date of this Act; nor shall the prohibitions in this section apply to investment securities of the kinds and amounts eligible for investment by national banks under the provisions of Section 5136 of the Revised Statutes. If, while such bank or bank holding company owns or controls such shares, securities or other obligations, the Board, after notice and opportunity for hearing, determines that the ownership or control of such shares, securities or obligations is being employed as a device for avoiding the provisions of this Act, it may by order require such bank or bank holding company to dispose of all or any part thereof forthwith."

Amend Section 6 as follows:

Change the figure "10" on page 8, line 10, to the figure "15".

Insert the following after the period on page 8, line 15:

"Provided, however, that nothing herein contained shall be construed to apply to the acquisition by a bank holding company of any additional voting shares of a bank in any case where such bank holding company, prior to such acquisition, owned a majority of the voting shares thereof."

Add the following to subsection (d) on page 9:

"Provided, however, that nothing herein contained shall be construed to authorize the approval of any acquisition subject to paragraphs (a), (b), or (c) of this section where, regardless of its competitive or other aspects, the effect of such acquisition may be to expand the size and extent of a bank holding company system beyond limits consistent with adequate and sound banking. The factors stated in this section shall likewise be considered by the Board, the Comptroller of the Currency or the Federal Deposit Insurance Corporation in determining whether to approve an application of any bank, which is a part of a bank holding company system, to establish a branch or branches of such bank."

Amend Section 7 as follows:

Add the following after the period on page 9, line 23:

"Provided, however, that any bank may, with the prior approval of the Board, accept such capital stock as a security for debts previously contracted."

Change the figure "10" to the figure "20" on page 10, line 12.

Add the following sentence after the period on page 10, line 13:

"Noninterest-bearing deposits to the credit of a bank shall not be deemed to be a loan or advance to the bank of deposit, nor shall the giving of immediate credit to a bank upon uncollected items received in the ordinary course of business be deemed to be a loan or advance to the depositing bank."

Amend Section 9 as follows:

Substitute the word "book" for the word "par" appearing on page 12, line 8.

Strike the words "and to eliminate losses and depreciation from the assets of such banks," appearing on page 12, lines 17 and 18, and substitute the following:

"and, with the permission of the Board, to increase the capital or surplus of its subsidiary banks and to eliminate losses and depreciation and to remove undesirable assets from the assets of such banks,"

Amend Section 13 as follows:

Change the figure "10" appearing on page 21, line 20, to the figure "9".

Amend paragraph (g) by adding before the quotation marks appearing on page 22, line 19, the following: ", or any subsidiary thereof as defined in said Act."

Add new paragraph at the end of line 19 on page 22 as follows:

"(h) Subsection (b) of Section 2 of the Banking Act of 1933, as amended, is amended by adding the following paragraphs:

"(4) which owns or controls, directly or indirectly, either a majority of the shares of capital stock of a member bank or more than 50 per centum of the number of shares voted for the election of directors of any one bank at the preceding election, or controls in any manner the election of a majority of the directors of any one bank; or

"(5) for the benefit of whose shareholders or members all or substantially all of the capital stock of a member bank is held by trustees."

May 29, 1947

To the Members of the  
Federal Advisory Council:

Following receipt of the mimeographed amendments submitted by the Federal Reserve Board, I talked over the phone today with Leonard Townsend.

He said:

1. That an amendment to provide tax exemption in case of compulsory divestments of non-banking assets would be introduced and is now in the process of being cleared with the Treasury;
2. That an additional amendment would be introduced at the suggestion of the Treasury which would require the Comptroller of the Currency, the Federal Reserve Board or the F.D.I.C. in granting applications for branches to a bank which was owned by a holding company, even if it was the only bank owned by the holding company, to take into account the same factors in the new subsection (d) of Section 6.

I called Townsend's attention to what I regarded as an ambiguity in the amendment adding a new subsection (d) to Section 5, in that it might by implication affect a bank which was not a holding company and give the Federal Reserve Board power over the disposition of non-banking assets which might have been taken for debts previously contracted or otherwise lawfully acquired. He said there was no intention to do this and offered to add after the word "bank" in the third line of the proposed amendment, the words, "which is a holding company." This would straighten the matter out as far as I am concerned. It might not, however, satisfy certain banks which are holding companies, such as the Trust Company of Georgia.

Townsend told me that the Council's resolution either had been or would be formally filed and made of record in the Senate Committee's hearings, and that the resolution of the Association of Reserve City Bankers was already filed.

E. E. Brown