A meeting of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System in Washington on Tuesday, January 26, 1937, at 2:45 p. m.

PRESENT: Mr. Eccles, Chairman
Mr. Harrison, Vice Chairman
Mr. Broderick
Mr. Szymczak
Mr. McKee
Mr. Ransom
Mr. Davis
Mr. Fleming
Mr. McKinney
Mr. Schaller
Mr. Hamilton

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

Reference was made to a meeting yesterday afternoon of members of the Board of Governors of the Federal Reserve System and the Presidents of the Federal reserve banks during which Messrs. Goldenweiser and Williams discussed the present credit and business situation and the question whether action should be taken by the Federal Reserve System to reduce the existing amount of excess reserves of member banks. At that time Mr. Goldenweiser reviewed the growth of the excess reserves of member banks, the possible credit expansion based on the present volume of reserves, and what the situation would be with respect to credit expansion if action were taken increasing reserve requirements 33 1/3%, or to double the statutory requirements. He also referred to the feeling that some action by the Federal Reserve System to absorb a substantial portion of existing excess reserves was necessary and stated that it appeared to him that the problems before the System were (1) what form that action should take and (2) the timing of such action. In connection with the latter point, he discussed various occasions in the past when action reversing existing policy, or in line with an agreed policy, had not been taken at the proper time or not vigorously enough, as illustrative of the utmost importance of proper timing of System action. He stated that an increase in reserve requirements would not constitute a reversal of the present easy money policy but would place the System in a position to exert an influence on the money market through operations in the System Open Market Account.

In considering whether action should be taken at this time, Mr. Goldenweiser said, the System was confronted with a different situation from that which existed last July when action was taken by the Board to increase reserve requirements, in that excess reserves were larger at that time, it did not appear then that the action would have any material effect upon money rates, and there was at that time a possibility of further increases in excess reserves resulting from gold imports.

He also discussed the present volume of industrial production and employment and other indications that recovery was well advanced and much stronger than when action was taken by the Board to increase reserve requirements in July, and said that the principal reasons for doubt as to whether action should be taken at this time were the continued volume of unemployment and labor troubles now present and in prospect.

He then expressed the opinion that the most effective time for action to prevent the development of unsound and speculative situations is in the early stages of such a movement when the situation is still susceptible of control, and that, as present indications were that such a time had arrived, as the technical market situation is favorable for action at the present time, and as short-term rates had been abnormally low in relation to long-term rates and some stiffening of the former would be desirable, action to absorb excess reserves should be taken at this time.

In connection with the question of the form that System action should take, if and when action is decided upon, Mr. Goldenweiser said he felt that in the course of the next year or more the System would be called upon to use more than one of the available instrumentalities to decrease excess reserves; and that, if it were going to be necessary sooner or later to increase reserve requirements, such action should be taken at a time when the banks could meet the increased requirements without substantial difficulty, as is the case at the present time. A survey recently completed by the Board, Mr. Goldenweiser said, showed that excess reserves of member banks, which totalled approximately $2,100,000,000 (approximately $600,000,000 more than the amount required to meet a 33 1/3% increase in reserve requirements), were generally well distributed among groups of banks; that all but 2,435 banks had sufficient balances at the Federal reserve banks at the present time to meet such an increase, and that all but 197 of these banks could furnish the required additional reserves by a transfer of not more than 50% of their balances with correspondent banks. He also stated that the 197 banks would have a deficiency in reserves of approximately $123,000,000, and that, while 168 of these banks were country banks, 149 of which were located in the Boston, New York, Philadelphia and Cleveland districts, these 168 country banks would have a reserve deficiency of only $2,349,000.

In discussing the objection that had been raised to an increase in reserve requirements that such action would deprive the member banks of additional earning assets, Mr. Goldenweiser stated that this would be true only in the case of a few banks which would find it necessary to dispose of earning assets to meet reserve requirements and that in all other cases the increase would result in the segregation as required reserves of idle funds of member banks on which no return was being received, and which had originated largely from gold imports.

In connection with the suggestion that a further increase in reserve requirements would result in the requirements of member banks being substantially higher than requirements in the various States for nonmember banks, Mr. Goldenweiser said that a study had been made recently of this matter, that the statutory requirements were confusing and difficult to compare, but that it appeared probable that, while the required reserves of member banks would be higher than the legal requirements for nonmember banks in most states, the difference in reserves actually maintained would not be very great when cash in vault and balances with other banks were taken into consideration. He also observed that the study indicated that the States with the smallest number of member banks were not the States with the lowest reserve requirements for nonmember banks and that it did not appear that reserve requirements were the determining factor in the decision of State banks to become members or to retain membership in the Federal Reserve System.

With respect to a suggestion as to country banks that there should be no increase in reserve requirements, or a smaller increase than in the case of reserve city banks, Mr. Goldenweiser said that these banks as a group had a large aggregate amount of excess reserves and excess balances with correspondents and could easily meet the increased requirements. An exemption of time deposits from an increase in reserve requirements, Mr. Goldenweiser said, had been suggested, but such an exemption should not be made as it would result in an increase in the actual differential between the reserve requirements for time and demand deposits and was undesirable for that reason. Whether time deposits are money or not was a subject of controversy among economists, but, he pointed out, the Federal Reserve System has supervisory and administrative as well as monetary responsibilities, is interested in the assets of banks as well as in their liabilities, and, therefore, cannot ignore time deposits, which, together with demand deposits, provide the funds for their loans and investments.

He then expressed the opinion that an increase in reserve requirements by 33 1/3% at this time would not involve a great risk on the part of the Federal Reserve System, and that this action would place the System in closer touch with the money market where it could influence the market by other means and would restore the System to the position in relation to the market which it normally should occupy.

Following Mr. Goldenweiser's statement Mr. Williams had stated that he felt the business and economic situation in the United States had reached what might be regarded in a general way as normal and that there were some indications that in certain respects it was going beyond a normal state. That being the case, he said, and in view of the emergency atmosphere which has been a factor in the consideration of problems during the years of the depression, it was necessary that the System keep its perspective of what the normal situation should be. He also expressed the opinion that prior to the depression a total of $500,000,000 of excess reserves would have been regarded as an unprecedented factor in the credit situation, that this should be borne in mind in dealing with the present problem, and that some action should be taken as promptly as possible to absorb the existing substantial amount of excess reserves, which should not be held under normal conditions. In referring to the question whether action should be taken in the face of existing labor troubles, Mr. Williams expressed the opinion that, while the strikes which are now in progress may delay full recovery, they would not destroy recovery and that, therefore, they did not present a sufficient reason for inaction by the System.

While it might prove to be the case, Mr. Williams said, that some banks would have to borrow to meet an increase in reserve requirements at the present time, he felt this problem could be met by them without a substantial amount of borrowing in the aggregate, and that the longer action by the System was delayed the greater would be the likelihood that the action which would be required at a later date would produce the necessity for liquidation by member banks. He agreed with the statement made by Mr. Goldenweiser that the most serious errors made in the past were the cases where action was too long delayed while waiting for a more favorable occasion for action, or was not sufficiently vigorous, and stated that he believed the System was confronted today with the danger of delaying action too long in the face of a business situation which was daily becoming more active.

Mr. Williams concluded with the statement that it appeared that there was every argument for early action by the System, that he felt that the Board should increase reserve requirements to the limit of its authority, and that this would place the System in a position to deal effectively with the problems which would arise later in connection with the control of credit through the medium of open market operations.

In response to an inquiry by the Chairman at this meeting, Mr. Goldenweiser stated that he desired to offer the further suggestion at this time that, in the event action was taken by the Board of Governors to increase reserve requirements, it would be highly desirable for the Federal reserve banks to reduce their buying rates on acceptances inasmuch as the existing rates were out of touch with the market, and, if an increase in reserve requirements should result in member banks having to resort to the Federal reserve banks for additional funds, they might wish to sell acceptances instead of borrowing in the form of rediscounts.

Mr. Williams stated that the only additional comment he wished to make at this time was that, as it was thought that if the Board raised reserve requirements to the extent of its remaining authority such action might result in some increase in short-term money rates, he felt it would be confusing if acceptance or discount rates were reduced, that such action might be interpreted as an indication that the System had a policy of maintaining the present low short-term rates, and that he felt it would be desirable to defer a decision in that direction until the effect of any action that might be taken by the Board can be determined, particularly in view of the fact that such action might result in market rates being increased to a point where the present rates of the Federal reserve banks on acceptances would attract bills.

Consideration was given to drafts of minutes of the meeting of the Federal Open Market Committee held on November 19, 1936, and an agreement was reached upon a revised form.

Upon motion duly made and seconded, the minutes were approved unanimously.

In connection with the consideration of the draft of minutes of the meeting of the Federal Open Market Committee held on November 20, 1936, which was sent to the members of the Committee on January 21, 1937, Mr. Harrison stated that it had been his understanding that the resolution with respect to granting authority to the Federal reserve banks to buy and sell cable transfers, and bills of exchange and bankers acceptances payable in foreign currencies, had been adopted in somewhat different form from that set forth in the draft.

The point was discussed and the resolution was approved in the following form:

"RESOLVED that, unless and until the Federal Open Market Committee hereafter directs otherwise, each Federal Reserve Bank, subject to the provisions of Section 14 of the Federal Reserve Act as amended and the regulations, conditions, and limitations of the Board of Governors prescribed thereunder, may without further directions or authorization of the committee purchase and sell, at home or abroad, cable transfers, and bills of exchange and bankers acceptances payable in foreign currencies, to the extent that such purchases and sales may be deemed to be necessary or advisable in connection with the establishment, maintenance, operation, increase, reduction or discontinuance of accounts of Federal Reserve Banks in foreign countries."

Upon motion duly made and seconded, the minutes of the meeting were approved unanimously as changed.

The Secretary submitted the minutes of the meetings of the executive committee of the Federal Open Market Committee held on November 19, November 20 and December 21, 1936, and, upon motion duly made and seconded and by unanimous vote, the actions set forth therein were approved, ratified, and confirmed.

It was stated that, pursuant to the authority granted by the Federal Open Market Committee at its last meeting and in accordance with instructions issued by the executive committee thereunder, the Federal Reserve Bank of New York had readjusted the participations of the Federal reserve banks in the System Open Market Account, as of January 1, 1937, in accordance with the plan and procedure followed in connection with the adjustment which was made as of October 1, 1936.

Upon motion duly made and seconded, and by unanimous vote, the readjustment was approved, ratified and confirmed and the executive committee was authorized to make a quarterly readjustment of the participations of the Federal reserve banks in the System account, as of April 1, 1937, in accordance with the same plan and procedure.

Prior to this meeting, Mr. Burgess as Manager of the System Open Market Account had sent to the members of the Federal Open Market Committee, under date of January 21, 1937, a report, prepared by the Federal Reserve Bank of New York, of open market operations since the last meeting of the Federal Open Market Committee on November 20, 1936, which operations had been reported in detail in the usual weekly reports. Mr. Burgess reviewed the contents of the report and the reasons for the transactions referred to therein.

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

Mr. Burgess then stated that, pursuant to the understanding reached at the meeting of the Presidents' Conference on November 18, 1936, the Presidents had transmitted to President Harrison their comments with respect to the proposed revised accounting procedure for the System Open Market Account and that, after consideration of the comments and consultation with Mr. Smead, Chief of the Board's Division of Bank Operations, the revised procedure was made effective as of January 1, 1937.

> Upon motion duly made and seconded, and by unanimous vote, the revised procedure, as outlined in the memorandum, dated November 19, 1936, submitted by Mr. Harrison at the Presidents' Conference, a copy of which is in the files of the Federal Open Market Committee, was approved and its application to the System Open Market Account as of January 1, 1937, was approved, ratified and confirmed.

Mr. Burgess stated that the principal question raised by the Presidents of the Federal reserve banks in connection with the revised accounting procedure related to the treatment of profits from sales, and premiums paid in connection with purchases of securities in the market, which presented the question whether the present practice of selling maturing issues in the market and replacing them with other securities purchased in the market should be continued or whether it would be possible to make direct exchanges with the Treasury of maturing securities for new issues.

In connection with the consideration of this matter, reference was made to an opinion submitted by Mr. Dreibelbis under date of January 26, 1937, in which it was stated that, after reviewing the provision permitting obligations of the United States to "be bought and sold without regard to maturities but only in the open market", in the light of its legislative history, its purpose as revealed thereby, and the various factors involved in effecting exchanges of old obligations for new ones and applying thereto ordinary rules of statutory construction, it was the conclusion of Mr. Dreibelbis that exchanges permitted under the Treasury circulars might be effected. Mr. Burgess stated that Counsel for the Federal Reserve Bank of New York had considered the question and had reached the same conclusion.

During the ensuing discussion, it was pointed out that the present practice resulted in the payment during 1936 of something in excess of $25,000 as commissions in connection with the purchase and sale of securities which otherwise might be exchanged without such expense and created the problem of the treatment to be given to profits on securities sold and premiums paid on securities purchased in the market, all of which would be avoided if direct exchanges with the Treasury were made. It was also stated that such exchanges would be confined to the replacement of maturing securities with securities of an issue being offered to the public under terms which permit the tender of the maturing securities in exchange.

> Upon motion duly made and seconded, it was agreed unanimously that, whenever such action appeared to be desirable in the proper administration of the System account, the Federal Reserve Bank of New York might exchange directly with the Treasury Department maturing securities held in the account for securities of an issue being offered to the public under terms which permit the tender of the maturing securities in exchange.

Consideration was then given to the proposal submitted by Mr. Harrison at the meeting of the Federal Open Market Committee on March 19, 1936, that authority be granted by the Committee under which, in an emergency, any Federal reserve bank might purchase Government securities when necessary to afford relief in a situation involving specific banking institutions in its district, or, after obtaining the consent of the Federal Open Market Committee, might purchase or sell Government securities for its own account, all of such purchases and sales to be reported promptly to the Federal Open Market Committee and its executive committee. Action on this proposal had been deferred at the meetings of the Committee on May 25 and November 20, 1936. In connection with this matter reference was made to the following letter addressed by President Harrison to each of the members of the Federal Open Market Committee under date of January 19, 1937:

> "Under the regulations of the Federal Open Market Committee, as it existed under the Banking Act of 1933, the individual Reserve banks were given power to purchase government

"securities for their own account in emergencies and subject to certain restrictions. The preliminary draft of regulations of the new Federal Open Market Committee, created by the Banking Act of 1935, included similar provisions; but when the regulations were adopted, at the first meeting of the committee on March 18 and 19, 1936, the section containing these provisions was omitted, with the understanding that any authority of this sort which was finally agreed upon would be conferred by action of the committee rather than by regulation, and the discussion of committee action on the matter was postponed until a later meeting.

"The subject was again discussed at the meetings on May 25, 1936 and on November 20, 1936. Action was postponed at the meeting on November 20 with the understanding that I should submit to the members of the committee in advance of the next meeting an outline of my suggestion as to an appropriate form of resolution.

"I have always believed, and I presume that other members of the committee, believe, that it is important that the Federal Reserve System be prepared to act promptly in any emergency which may arise. Indeed, one of the reasons for the reorganization of the Open Market Committee was to concentrate responsibility and to facilitate action. Prompt action in matters of credit policy is provided for either under existing regulations or resolutions. There is doubt, however, as to whether the appropriate machinery is available to take care of a pressing emergency involving individual member or non-member banks. Ordinarily, it is no doubt true that there will be adequate opportunity for any Reserve bank which faces an emergency situation to get in touch with the executive committee and to arrange, through that committee, any purchase of government securities which may be necessary. It is also true, however, that on a number of occasions in the past events have taken place so rapidly that adequate opportunity was not available for committee action of that sort. It is not impossible that such a situation may recur in the future.

"I believe, therefore, that it is important that some standing authority for emergency action by individual banks should be granted not only that the banks may be in a position to meet the emergency, but also that there may be no basis for a charge that the System is not prepared to act promptly and vigorously on all occasions.

"The following resolution would seem to me adequate to remove any obstacle to immediate functioning of the Reserve machinery in an emergency and would at the same time preserve to the Open Market Committee its substantial rights of control over open market operations:

In an emergency, when necessary to afford relief in a situation involving one or more specific banking "institutions in its district, any Federal Reserve bank may purchase government securities for its own account (a) up to and not in excess of $100,000,000 with the prior consent of the executive committee, or (b) up to and not in excess of $50,000,000 without the prior consent of the executive committee, if because of the necessity for prompt action it is not possible to obtain such prior consent.

All purchases of government securities by any Federal Reserve bank for its own account shall be reported promptly to the executive committee; and the executive committee shall promptly notify all members of the Federal Open Market Committee of such purchases. The Federal Open Market Committee reserves the right, and authorizes the executive committee, at any time to require the sale of any government securities purchased by an individual Federal Reserve bank for its own account, or to require that such securities be transferred to the System Open Market Account, or to reduce the holdings of other government securities in the System Open Market Account in an equivalent amount.

"In accordance with the understanding at the last meeting of the Open Market Committee that I should present my views to each member of the committee, I am taking the liberty of sending a copy of this letter to each member of the Board of Governors and to those Presidents who are members of the Open Market Committee."

Chairman Eccles stated that the responsibility for open market operations was vested in the Federal Open Market Committee, that the Federal reserve banks, through the exercise of their powers to make loans and resale agreements, had ample authority to deal with specific local situations which might arise without warning, that in all other cases the banks would have sufficient notice of the development of the situation to bring the matter to the attention of the executive committee of the Federal Open Market Committee for consideration and action; that, under these circumstances, there was no justification, in his opinion, for granting the authority referred to by Mr. Harrison; and that he was opposed in principle to granting the authority.

During the discussion which followed Mr. Broderick suggested that the limits set forth in Mr. Harrison's proposal might be reduced to substantially lower figures. There was also raised a question whether the adoption of Mr. Harrison's proposal would involve a delegation to the Federal reserve banks of the Committee's authority. In response to an inquiry, Mr. Dreibelbis expressed the view that it was within the power of the Committee to adopt the proposed resolution.

At the conclusion of the discussion, Mr. Harrison moved the adoption of the following resolution for the reasons outlined in his letter of January 19:

"RESOLVED that, in an emergency, when necessary to afford relief in a situation involving one or more specific banking institutions in its district, any Federal Reserve bank may purchase government securities for its own account (a) up to and not in excess of $100,000,000 with the prior consent of the executive committee, or (b) up to and not in excess of $50,000,000 without the prior consent of the executive committee, if because of the necessity for prompt action it is not possible to obtain such prior consent. All purchases of government securities by any Federal Reserve bank for its own account shall be reported promptly to the executive committee; and the executive committee shall promptly notify all members of the Federal Open Market Committee of such purchases. The Federal Open Market Committee reserves the right, and authorizes the executive committee, at any time to require the sale of any government securities purchased by an individual Federal Reserve bank for its own account, or to require that such securities be transferred to the System Open Market Account, or to reduce the holdings of other government securities in the System Open Market Account in an equivalent amount."

Mr. Harrison's motion, having been duly seconded, was put by the chair and the members voted as follows:

"Aye"	"No"
Mr. Harrison	Mr. Eccles
Mr. Fleming	Mr. Szymczak
Mr. Schaller	Mr. Ransom
Mr. Hamilton	Mr. McKee
Mr. McKinney	Mr. Davis
Mr. Broderick	

Mr. Broderick then stated that he desired to withdraw his vote, that while he favored the adoption of the resolution, he believed that motions of this character, if adopted, should prevail by a larger margin than had been indicated in this case, and that, therefore, he wished to be recorded as not voting.

Thereupon the motion was declared lost.

Consideration was then given to the authority to be given to the executive committee to direct replacement of maturing securities and to make shifts between maturities of securities in the System Open Market Account and the opinion was expressed and concurred in that authority to direct the replacement of maturing securities and to make such shifts between maturities in the account as may be necessary in the proper administration of the account should be granted and that, for the reasons which prompted the granting of the authority at the meeting of the full Committee on November 20, 1936, the same authority should be granted at this meeting.

Upon motion duly made and seconded, and by unanimous vote, the Committee instructed the executive committee to direct the replacement of maturing securities in the System Open Market Account with other Government securities and to make such shifts between maturities in the account as may be necessary in the proper administration of the account, provided that the amount of securities maturing within two years be maintained at not less than $1,000,000,000 and that

> the amount of bonds having maturities in excess of five years be not over $600,000,000 nor less than $300,000,000.

It was also agreed that, for the reasons stated at the meeting on November 20, 1936, the authority granted to the executive committee to permit fluctuations in the total holdings of securities in the System account between weekly statement dates should be continued.

> Upon motion duly made and seconded, and by unanimous vote, the Committee authorized the executive committee to permit such fluctuations, within reasonable limits, in the amount of holdings of Government securities in the System Open Market Account between wee ly statement dates as may be desirable for the practical administration of the account in making shifts between and replacements of securities pursuant to the general authority granted by the Federal Open Market Committee.

In connection with the consideration of the authority to be given to the executive committee to effect increases or decreases in the total holdings of securities in the account, Chairman Eccles referred to the possibility that the Board of Governors might decide to increase reserve requirements to take effect prior to March 15, 1937, the date upon which the first income tax payments for the year 1936 will be made, when it was anticipated that payments to and by the Treasury would result in a net withdrawal of funds from the market up to $500,000,000. He expressed the opinion that the executive committee should be in a position, should such a situation develop, to buy securities to offset any adverse effect that might result from such a large withdrawal of funds, with the understanding that the securities so acquired would be disposed of as the funds withdrawn were returned to the market.

Mr. Burgess stated that, as excess reserves would be very substantially reduced by an increase in reserve requirements if made to the full extent permitted by law, there would be less flexibility in the money market and that in such circumstances larger open market operations should be contemplated and authorized.

For these reasons, and the further reason that it was felt that the executive committee should have authority to take such action with respect to an increase or decrease in the system portfolio as might be necessary to meet unforeseen circumstances which might arise, it was agreed that enlarged authority should be granted to the executive committee to direct increases or decreases in the system portfolio.

> Upon motion duly made and seconded, and by unanimous vote, the Committee authorized the executive committee, subject to telegraphic or written approval by a majority of the members of the Federal Open Market Committee, to direct that the present amount of Government securities in the System Open Market Account be increased or decreased by not more than $500,000,000.

Reference was made to anticipated changes in the membership of the Federal Open Market Committee on March 1, 1937, and the question was presented what, if any, action should be taken by the Committee to fill any resulting vacancies in the membership and alternate membership of the executive committee.

> Mr. Fleming moved that the representative elected by the Federal Reserve Banks of Philadelphia and Cleveland as a member of the Federal Open Market Committee for the year beginning

March 1, 1937 be appointed to serve as a member of the executive committee for the period from March 1, 1937, until his successor is elected at the first meeting of the Federal Open Market Committee after March 1, 1937.

This motion, having been duly seconded, was put by the chair and carried unanimously.

Mr. Hamilton moved that the representative elected by the Federal Reserve Banks of Chicago and St. Louis to serve as a member of the Federal Open Market Committee for the year beginning March 1, 1937 be appointed an alternate member of the executive committee for the period from March 1, 1937, until his successor is elected at the first meeting of the Federal Open Market Committee after March 1, 1937.

This motion, having been duly seconded, was put by the chair and carried unanimously.

Mr. McKee moved that the Federal Open Market Committee take such action as may be necessary to reduce the amount of securities held in the System Open Market Account by approximately $800,000,000, and that it formally notify the Board of Governors of the Federal Reserve System of that decision.

There was no second to this motion and no action was taken upon it.

Mr. Harrison moved as a substitute for Mr. McKee's motion that the Chairman be requested to call a meeting of the Federal Open Market Committee on or before February 12, 1937; it being understood that, if the situation should change to such an extent that it appears unnecessary to hold a meeting at that time and the members of the Committee are in unanimous agreement that there is no need for a meeting, it could be dispensed with.

Mr. Harrison's motion, having been duly seconded, was put by the Chair and carried unanimously.

Thereupon the meeting adjourned.

Chester Morrill
Secretary.

Approved: M S Eccles
Chairman.