

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

September 18, 1942.

Governor Ransom:

I'm sorry that this did not reach you in time last night. I held it up in order to get the figures for this week, which were not available until four o'clock, and then some time was necessary for analysis, composition, and typing.

Woodlief Thomas.

Attachment

BOARD OF GOVERNORS  
OF THE  
FEDERAL RESERVE SYSTEM

# Office Correspondence

Date September 17, 1942

To Governor Ransom

Subject: Reserve Situation

From Woodlief Thomas

## Little change in total excess reserves

The general level of excess reserves for all member banks taken as a whole has shown little change since the latter part of June. There have been wide day-to-day and week-to-week fluctuations owing largely to variations in Treasury balances, but these fluctuations have been mostly within the range of between 2 billion dollars and 2.5 billion. As of yesterday (September 16) excess reserves were at a high level of 3 billion dollars, owing to an overdraft of the Treasury at the Reserve Banks, but this is only a temporary situation and before the end of the month the total will again be close to 2.5 billion dollars. The following table shows the factors and changes in member bank reserves and excess reserves from July 1 to September 16:

Factors Causing Changes in Excess Reserves  
(In millions of dollars)

	Outstanding Sept. 16, 1942	Change since July 1, 1942	
		Factors of increase	Factors of decrease
Reserve System open market account	3,384	+656	
Special Treasury certificate.....	189	+189	
Other Reserve Bank credit.....	284	+140	
Gold stock.....	22,747	+8	
Treasury currency.....	3,346	+32	
Money in circulation.....	13,440		+1,024
Treasury cash.....	2,206		+11
Treasury deposits with F.R.Banks..	6	-479	
Nonmember deposits.....	1,239	-102	
Other Federal Reserve accounts....	299		+2
Member bank reserve balances.....	12,760	+568	
Required reserves - total.....	9,720	-212	
Increase due to deposit growth...			+628
Decrease due to reduction in percentage requirements at central reserve city banks.....		-840	
Excess reserves--all member banks.	3,040	+780	
New York.....	624	+273	
Chicago.....	68	+15	
Other.....	2,348	+492	

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The continued and, in fact, accelerated expansion of money in circulation, amounting to over a billion dollars in past 11 weeks, has taken reserves from banks all over the country and there has also been a growth of over 600 million dollars in required reserves resulting from the steady expansion in deposits. These factors causing decreases in excess reserves have been offset by Federal Reserve action -- purchases of Government securities (660 million) and reduction in reserve requirements at central reserve city banks (about 840 million). In addition the decline in Treasury deposits at the Reserve Banks to nearly nothing, the Treasury overdraft of 190 million, and large Federal Reserve float on September 16 have temporarily added several hundred million to bank reserves.

#### Loss of reserves by New York

Forces drawing reserves from New York City have continued to operate and these banks, although benefiting mostly from Federal Reserve action, have been barely able to retain any excess reserves. They declined from around a billion dollars in the first quarter of this year to about 500 million dollars in May and June, and around 250 million in July and August, falling at times to below 200 million. At Chicago banks excess reserves have generally been below 100 million dollars since June. The most important of the factors drawing reserves from New York, as shown on Chart 1, has been the excess of Treasury receipts over disbursements in New York. These developments were discussed at some length in both the August and September Bulletins and are illustrated by the accompanying charts.

New York banks bought large amounts of Government securities in July and August and in addition there were substantial purchases by depositors of New York City banks of the 1962-67 bonds. All of these purchases built up war-loan deposit accounts at New York City banks to slightly more than 2 billion dollars on August 15. In the following month the Treasury drew heavily on these deposits. In the first two weeks of September, in view of their tight reserve situation, New York banks reduced somewhat their holdings of Governments.

The second decrease in reserve requirements added another 330 million dollars to New York City banks' excess reserves, and with the Treasury overdraft this week these banks on September 16 had 624 million dollars of reserves in excess of requirements. Payments for the new issue of Treasury certificates next Monday and for the new note issue on Friday, September 25, will be followed by additional large Treasury withdrawals. New York excess reserves will no doubt be well below 500 million dollars before the end of the month.

#### Little change outside New York

Banks outside New York have also had to meet large currency demands and increases in required reserves; they have purchased tremendous amounts of Government securities; but their excess reserves have shown little change. The Treasury has spent more funds in these regions than it has obtained there. The transfers from New York have enabled these banks to meet currency demands

and increased requirements without reducing excess reserves. The growth in bank deposits has been widespread, occurring in all districts and in places of various sizes, as shown in the table in the September Bulletin (p.875). While there are no doubt communities that have shown little or no gain, they do not seem to be centered in any particular regions.

#### Prospective future changes in reserves

It may be expected that the factors operating toward a decline in excess reserves will continue in the near future. The increase in money in circulation has risen from a monthly rate of 200 million dollars or less in the early part of this year to a rate of nearly 500 million within the past month. This increase is nation-wide and seems clearly to be related to the growth in incomes of people who do not have bank accounts -- a development that is likely to continue for some time.

The growth in deposits at banks and the resulting increase in required reserves will also continue. It is estimated that the Treasury will sell in the fourth quarter of this year about 11.5 billion dollars of marketable obligations. If member banks and Federal Reserve banks purchase 60 per cent of these, the rate that has prevailed recently, they will take about 7 billion. Continued withdrawals of currency, which should equal about 1 1/4 billion dollars, and a probable further decline in loans would partially offset the effect on bank deposits of the increase in security holdings. It is likely that demand deposits of member banks will increase by as much as 5 billion dollars in the quarter, with a resulting rise of one billion in required reserves.

The net result of the increase in currency and the growth in required reserves, barring further Federal Reserve action, would be a further decline in excess reserves to 200 or 300 million dollars by the end of the year. From April to the middle of August Federal Reserve open-market purchases approximately offset the increase in currency in circulation. It would seem desirable that open-market purchases should continue to be at least as large as the currency drain. With the bill buying rate and with the growing demand for reserves, something like that amount of bills will probably be offered to the System. A further decline of 2 per cent in reserve requirements at central reserve city banks would add another 400 million dollars to excess reserves. With such a reduction in requirements and System security purchases equal to the currency increase, the probable decline in excess reserves during the last quarter of the year would be about 600 million dollars, leaving a total volume at the end of the year for all member banks of 1.9 billion dollars.

#### Prospects for New York banks

It is difficult to estimate the trend of excess reserves in New York City because that will depend upon the action of New York City banks in purchasing securities. If they continue to purchase at the same rate as they have in recent months, they will quickly lose all of their excess reserves. Their ability to continue to buy will depend upon how many Treasury bills they sell to the Reserve Bank. You may recall that I asked Allan Sproul the other day

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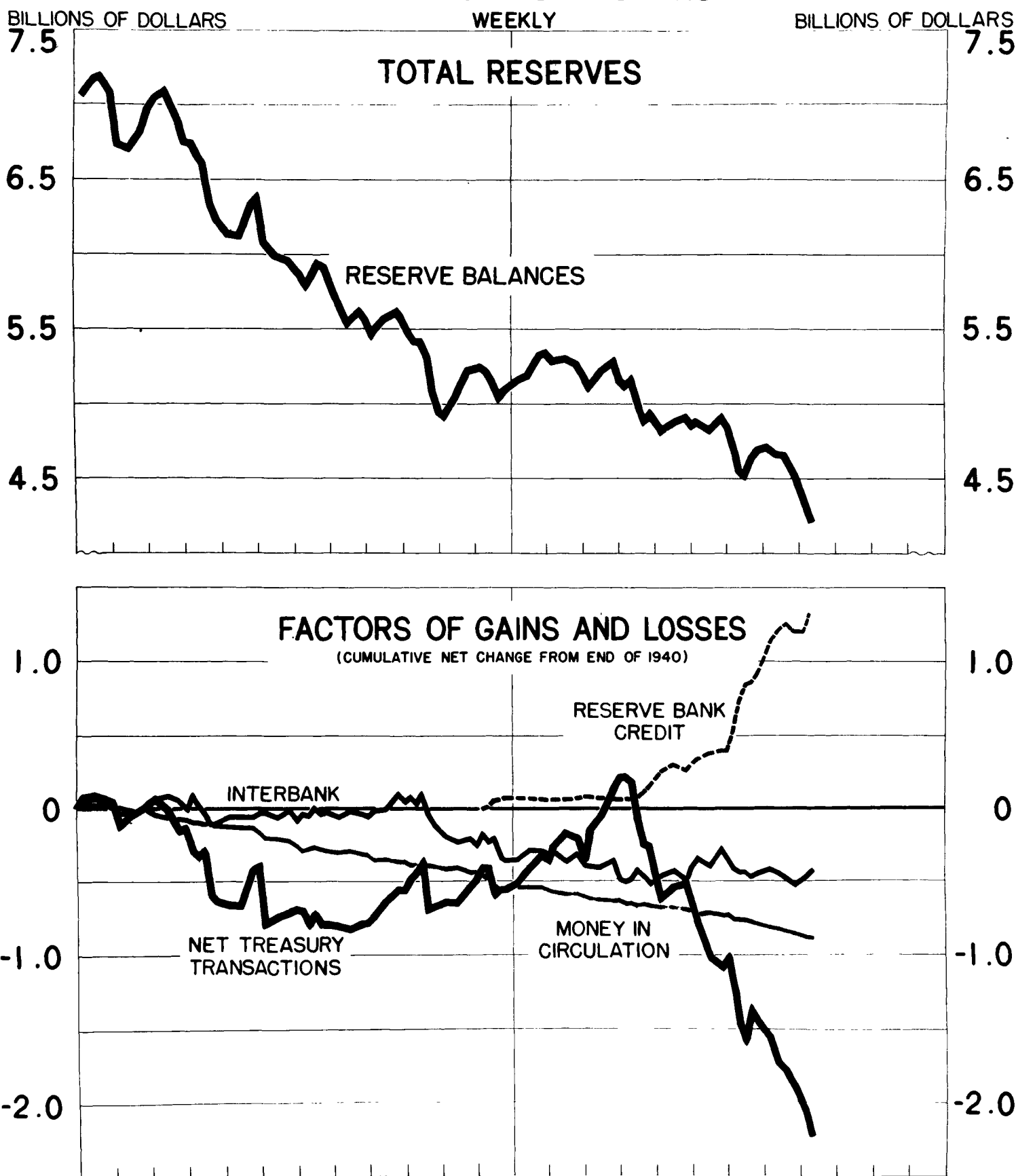
whether if New York banks had no excess reserves they would continue to bid for Treasury bills. His reply was that New York banks and New York dealers would continue to bid for new issues and if unable to dispose of them otherwise, or if the banks were short of reserves, they would sell the bills to the System. Under these conditions New York City banks are automatically supplied with such reserves as they need. It seems likely that in the future excess reserves in New York will generally be close to a minimum amount.

If the Treasury should offer a considerable volume of issues that appeal to investors outside New York it is likely that the drain of funds from New York would be diminished. The need for open-market operations by the System would then also be reduced because outside banks could meet increased reserve needs out of excess reserves already on hand. If purchases of Government securities at New York City banks are reduced and those of outside banks are increased, there may be some decline in excess reserves outside New York. There is nothing in the present situation, however, to indicate that this is taking place. The Treasury issues to be paid for next week are of such a nature that they are not likely to change the recent trend. It will be interesting to see whether securities to be issued in October, which presumably will be of longer term and bear higher rates, will have any affect on the situation.

W. T.

# FACTORS OF GAINS AND LOSSES OF RESERVE FUNDS

BY NEW YORK CITY BANKS

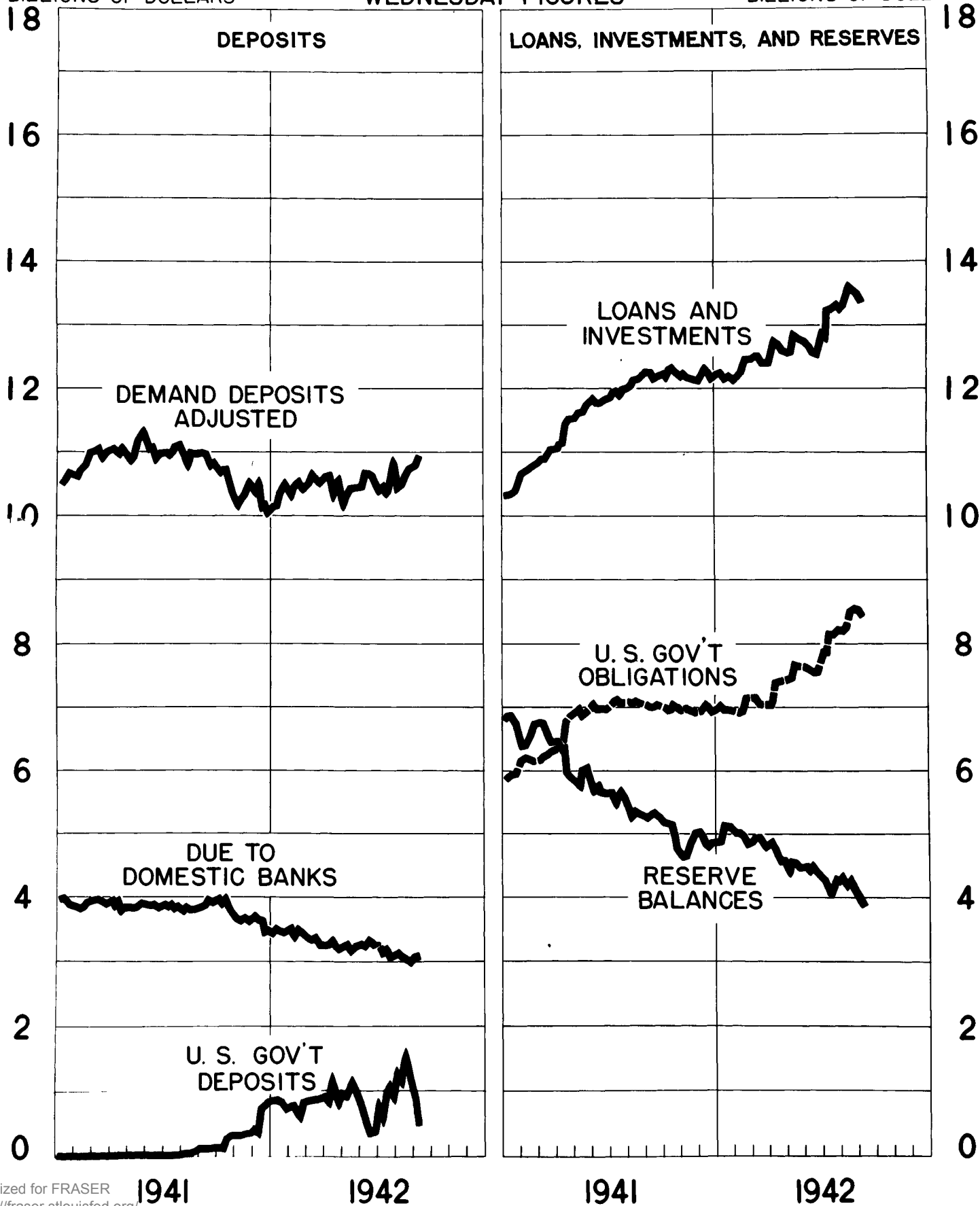


# REPORTING MEMBER BANKS IN NEW YORK CITY

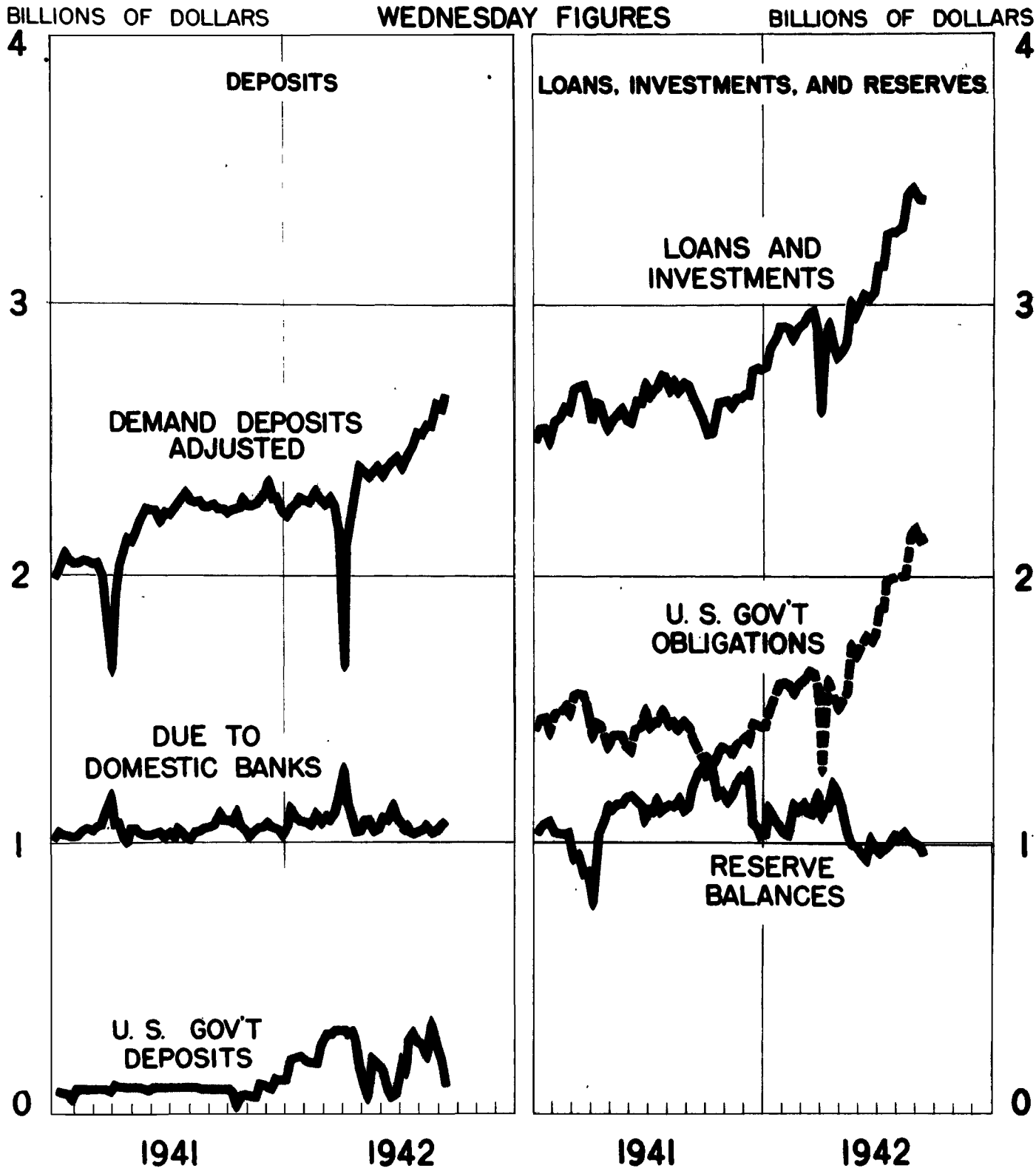
BILLIONS OF DOLLARS

WEDNESDAY FIGURES

BILLIONS OF DOLLARS



# REPORTING MEMBER BANKS IN CHICAGO

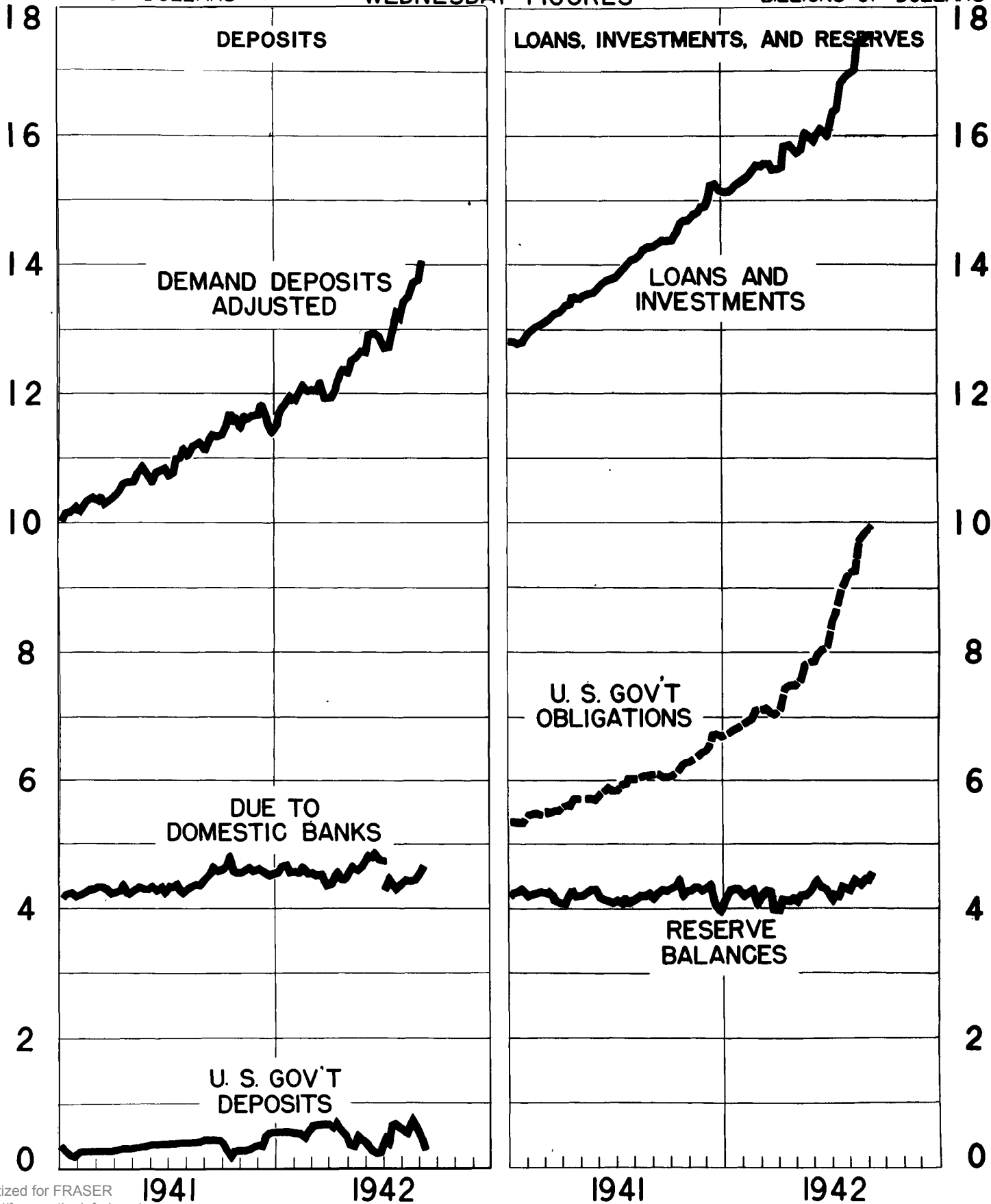


# REPORTING MEMBER BANKS IN 99 OTHER CITIES

BILLIONS OF DOLLARS

WEDNESDAY FIGURES

BILLIONS OF DOLLARS



# EXCESS RESERVES OF MEMBER BANKS

