

DIRECT PURCHASES OF GOVERNMENT SECURITIES BY FEDERAL RESERVE BANKS

MARCH 10, 1947.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. WOLCOTT, from the Committee on Banking and Currency, submitted the following

REPORT

[To accompany H. R. 2413]

The Committee on Banking and Currency, to whom was referred the bill (H. R. 2413) to amend the Federal Reserve Act, and for other purposes, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

GENERAL STATEMENT

At the present time the 12 Federal Reserve banks have the authority to purchase and sell any bonds, notes, or other obligations which are direct obligations of the United States or which are fully guaranteed by the United States as to principal and interest without regard to maturities directly from or to the United States. The aggregate amount of such direct purchases of Government securities which the 12 Federal Reserve banks are authorized to hold at any one time is limited to \$5,000,000,000. This authority to purchase and sell Government securities directly from or to the Treasury was granted by title IV of the Second War Powers Act, approved March 27, 1942, which amended section 14 (b) of the Federal Reserve Act, and the authority expires March 31, 1947. The Federal Reserve System had used this direct purchase authority without any limitation as to amount of holdings from the time of its creation in 1913 to 1935, when the National Banking Act of 1935 limited such purchases and sales of Government securities to open-market transactions. The existing authority to purchase Government securities directly from the Treasury up to \$5,000,000,000 was, as stated, provided by the Second War Powers Act, 1942, and facilitates the meeting by the Treasury of temporary needs when refunding large maturities of public debt at or near tax-payment periods without undue disturbance to securities or money markets and without requiring the Treasury to maintain excessively large cash balances at such times.

By providing this line of credit the Treasury has a source to which it may turn to obtain funds in a substantial amount on little notice to

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meet temporary situations and contingencies. With such an emergency source of funds, it is possible for the Treasury to operate with a smaller cash balance than might otherwise be necessary, thus resulting in a saving of interest. To obtain funds to meet such temporary requirements without direct purchases by the Federal Reserve banks, the Treasury would be obliged to arrange for the sale of securities to dealers in the market, with the assurance that the Federal Reserve banks would repurchase the securities; and this not only would be inconvenient and troublesome but would increase the expense without serving any useful purpose. Furthermore, direct buying provides a flexible method of easing the money market in periods of heavy drain as, for example, around income-tax dates. By borrowing funds from the Federal Reserve banks and expending them prior to tax dates, the Treasury can put the funds into the market; and, as taxes are received, such special borrowings are reduced and some retired. In this connection the direct purchase authority provides for efficient and businesslike management of the public debt.

Since the direct purchase authority was granted in 1942, it has been used only 61 days, all falling at periods when the Treasury had to meet large payments, generally for interest or for redemption of maturing debt, a few days before large tax receipts were deposited. The authority was not used in 1946, because the Treasury had large cash balances resulting principally from the proceeds of the eighth war-loan drive. As used to date, it has provided the Treasury with an authorized line of credit which it could use if needed and which, on use, has been secured by special one-day obligations on which the Government pays interest at the very nominal rate of one-quarter of 1 percent per annum. The 61 days this direct purchase authority has been used since 1942 is shown herewith by amounts and dates:

Direct purchase authority holdings of special short-term Treasury certificates by the Federal Reserve banks, 1942 to present

(In millions of dollars)

Date	Amount	Date	Amount
1942—June 16	58	1943—Mar. 18	836
June 19	70	Mar. 19	778
June 20	47	Mar. 20	768
June 22	34	Mar. 22	603
June 23	94	Mar. 23	700
Sept. 15	324	Mar. 24	512
Sept. 16	189	Mar. 25	432
Sept. 17	286	Mar. 26	384
Sept. 18	76	Mar. 27	304
Sept. 19	53	Mar. 29	104
Nov. 27	139	Mar. 30	40
Nov. 28	329	June 15	805
Nov. 30	422	June 16	659
Dec. 1	98	June 17	350
Dec. 10	16	June 18	256
Dec. 15	145	June 19	212
1943—Jan. 29	115	Sept. 8	11
Jan. 30	202	Sept. 9	126
Mar. 2	3	Sept. 10	243
Mar. 4	174	Sept. 11	246
Mar. 5	354	Sept. 12	214
Mar. 6	543	Sept. 14	179
Mar. 8	591	Sept. 15	424
Mar. 9	648	Sept. 16	258
Mar. 10	632	1945—Mar. 15	4
Mar. 11	790	Dec. 4	107
Mar. 13	1,043	Dec. 5	318
Mar. 15	1,302	Dec. 6	374
Mar. 16	1,250	Dec. 7	484
Mar. 17	981	Dec. 8	484
		Dec. 10	202

CONCLUSION

In view of the huge public debt, much of which is in short maturities requiring frequent refunding operations, and the desirability that the Treasury not be required to carry large cash balances which would increase the amount and cost of the public debt, the committee feels that the direct purchase authority limited to aggregate holdings at any one time of \$5,000,000,000 should be continued so that the temporary needs of the Treasury can continue to be met in an economical manner. The committee does not think it advisable that the direct purchase authority be made permanent, and so has provided for a termination of the authority on June 30, 1950. The committee feels that by providing for a termination of the authority on June 30, 1950, the Congress could at that time review the necessity for its continuance for a longer period if such might be its desire and conditions so warranted. The committee further feels that it is advisable to require the Board of Governors of the Federal Reserve System to include in its annual report to the Congress a detailed statement regarding such direct purchases and sales so that the Congress and others interested will have an annual review of its use. Such statement by the Board of Governors in its annual report will be so indexed as to be readily identified as direct purchases of Government securities under this authority and will show its cumulative use since 1942. In effect, two reviews of the use of the direct purchase authority will thus be afforded the Congress—an annual review as reported in the annual report of the Board of Governors of the Federal Reserve System, and an automatic review in view of the termination of the authority on June 30, 1950.

The bill would amend section 14 (b) of the Federal Reserve Act so that, until July 1, 1950, the 12 Federal Reserve banks could buy and sell either in the open market or directly from or to the United States any bonds, notes, or other obligations which are direct obligations of the United States or which are fully guaranteed by the United States as to principal and interest, but that the aggregate amount of such obligations acquired directly from the United States which is held at any one time by the 12 Federal Reserve banks shall not exceed \$5,000,000,000 and that the Board of Governors of the Federal Reserve System shall include in their annual report to Congress detailed information with respect to such direct purchase and sales.

The bill further provides, in view of the fact that the proviso in section 14 (b) of the Federal Reserve Act also contains the authority of the Federal Reserve bank to purchase and sell Government securities in the open market, that after June 30, 1950, when the direct purchase authority would terminate, the purchase and sale of Government obligations could continue to be made but only in the open market.

CHANGES IN EXISTING LAW

In compliance with paragraph 2a of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as introduced, are shown as follows (existing law proposed to be

omitted is enclosed in black brackets, new matter is printed in italics, existing law in which no change is proposed is shown in roman):

FEDERAL RESERVE ACT

* * * * *

SEC. 14. Any Federal Reserve bank may, under rules and regulations prescribed by the Board of Governors of the Federal Reserve System, purchase and sell in the open market, at home or abroad, either from or to domestic or foreign banks, firms, corporations, or individuals, cable transfers and bankers' acceptances and bills of exchange of the kinds and maturities by this Act made eligible for rediscount, with or without the endorsement of a member bank.

Every Federal reserve bank shall have power:

(a) To deal in gold coin and bullion at home or abroad, to make loans thereon, exchange Federal reserve notes for gold, gold coin, or gold certificates, and to contract for loans of gold coin or bullion, giving therefor, when necessary, acceptable security, including the hypothecation of United States bonds or other securities which Federal Reserve banks are authorized to hold;

(b) To buy and sell, at home or abroad, bonds and notes of the United States, bonds of the Federal Farm Mortgage Corporation having maturities from date of purchase of not exceeding six months, bonds issued under the provisions of subsection (c) of section 4 of the Home Owners' Loan Act of 1933, as amended, and having maturities from date of purchase of not exceeding six months, and bills, notes, revenue bonds, and warrants with a maturity from date of purchase of not exceeding six months, issued in anticipation of the collection of taxes or in anticipation of the receipt of assured revenues by any State, county, district, political subdivision, or municipality in the continental United States, including irrigation, drainage and reclamation districts, such purchases to be made in accordance with rules and regulations prescribed by the Board of Governors of the Federal Reserve System: Provided, That, *notwithstanding any other provision of this Act, (1) until July 1, 1950, any bonds, notes, or other obligations which are direct obligations of the United States or which are fully guaranteed by the United States as to principal and interest may be bought and sold without regard to maturities either in the open market or directly from or to the United States; but all such purchases and sales shall be made in accordance with the provisions of section 12A of this Act and the aggregate amount of such obligations acquired directly from the United States which is held at any one time by the twelve Federal Reserve banks shall not exceed \$5,000,000,000; and (2) after June 30, 1950, any bonds, notes, or other obligations which are direct obligations of the United States or which are fully guaranteed by the United States as to principal and interest may be bought and sold without regard to maturities but only in the open market. The Board of Governors of the Federal Reserve System shall include in their annual report to Congress detailed information with respect to direct purchases and sales from or to the United States under the provisions of the preceding proviso.*

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MINORITY VIEWS

H. R. 2413 seeks to extend an emergency war power which is totalitarian in concept and potentially highly inflationary in its effects. The bill should be defeated.

This measure, known as the Wolcott bill, would extend until 1950 that part of the Second War Powers Act which authorizes the Treasury to borrow directly from the Federal Reserve banks. This is the classical route to uncontrolled inflation.

Mr. Eccles, Chairman of the Board of Governors of the Federal Reserve, the only witness to appear before the committee, said the limit of funds permitted to be raised by the Treasury under this bill should be ten billion dollars instead of five, as provided in the pending bill, and that the legislation should be made permanent as provided in the first Wolcott bill, H. R. 2233.

Mr. Eccles testified that the purposes of this bill were to provide the Treasury with an overdraft arrangement. As he expressed it, the bill would give the Treasury "a line of credit on which it can call at a moment's notice," and to meet conditions where "the market situation was not satisfactory or favorable."

Mr. Eccles further urged the bill "for any purpose that was in the interest of Government to use it" and to avoid "idle balances" in the Treasury. Putting it in everyday English, what Mr. Eccles wants and this bill would O. K., is Treasury power to issue fiat money to pay its bills—whenever its actions have exhausted public confidence.

Since the beginning of time, political rulers, when expenditures have exceeded tax collections, have regularly resorted to manufacturing money by one process or another. This measure is the latest of those attempts at "push button" money.

Sugar-coating this proposal with promises that the power requested is only for a limited period to meet a passing need, and that it will never be abused but always used wisely, in no way changes its inflationary nature.

The minority urges the Members of the House to appraise this scheme in the light of history. We should also try to judge the contents of the bill not alone by its own inflationary effects but also by its potentialities and cumulative impetus which it gives to the smouldering inflationary fires threatening our entire economy.

This measure would give encouragement to the reckless spenders and the Truman budget advocates. It would provide them with an automatic instrument for accelerating inflation. Naturally, all of those elements in and out of Congress favor the Wolcott bill.

The crushing burdens of inflation always fall most heavily upon the laboring people and poor, upon those of unquestioning faith in their Government. In simple justice to these humble people we urge our colleagues to protect them from this short-cut route to ruinous all-out currency inflation and the terrifying consequences that would follow.

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HOWARD BUFFETT