

Restoration of the previous ratio of required gold certificate reserves held by Federal Reserve Banks of 40 per cent against Federal Reserve notes and 35 per cent against Federal Reserve Bank deposits has been proposed to your Committee as an anti-inflationary measure. This proposal would make no contribution whatever to the fight against inflation. It would not sterilize new acquisitions of gold nor would it give the Federal Reserve System any additional powers to curb inflationary expansion of bank credit.

The present reserve requirements of the Federal Reserve Banks stand at a uniform level of 25 per cent. Congress established them at this level in consequence of the wartime expansion of currency and Reserve Bank credit. The previous requirements of 40 per cent against notes and 35 per cent against deposits, incorporated in the Federal Reserve Act of 1913, were largely arbitrary.

To restore the prewar levels now would only entail needless operating difficulties for some of the Federal Reserve Banks. The combined Banks at present hold gold certificates amounting to 50.6 per cent of their total note and deposit liabilities, or approximately 6 billion dollars in excess of the proposed higher requirements. Thus, they would not prohibit Reserve Banks from providing member banks with additional funds on which to base a considerable further expansion of bank credit.

If Reserve Banks were to be prevented by this device from issuing currency and member banks were thus unable to supply currency to their customers, it would precipitate the kind of money panic which the Federal Reserve System was created to prevent. Likewise, if the Federal Reserve System, because of an artificial limitation, were unable to supply credit

to member banks, the results could well be demoralizing in the Government bond market.

Although the Reserve System as a whole has gold certificate reserves in excess of the proposed higher requirement, there is considerable variation among individual Federal Reserve Banks. The requirement applies to each of the twelve Reserve Banks. As a practical operating matter, these Banks cannot permit the ratios to go down to the vanishing point and hence require a working margin of at least 3 per centage points. If the higher requirement were restored, some Federal Reserve Banks would have a substantial deficiency, others would be below or close to the necessary operating margin, while still others would have a large excess. Reserve Banks with a deficiency would be obliged to sell some of their Government securities to or to borrow from Reserve Banks which had an excess. The reserve position of the individual Federal Reserve Banks is constantly changing with seasonal and other movements of funds in the economy. Therefore, the proposal would entail operating difficulties and constant inconvenience without accomplishing any useful purpose.

Expansion or contraction of Reserve Bank credit should be determined by the needs of the economy and not by the amount of gold certificates which Reserve Banks happen to have, which in turn is contingent upon international movements of gold. Likewise, inability to supply credit to member banks would compel the System to withdraw support from the Government securities market and perhaps even to sell securities which it now holds at whatever prices or yields they would bring in the market.

The Reserve Banks do not control the amount of currency which the public wishes to hold. It is the depositors of the banks and the recipients of checks who determine the volume of outstanding currency. They create the demand and member banks come to their respective Federal Reserve Banks to obtain such amounts of currency as their depositors or others presenting checks may desire to have.

If the Reserve System were unable to meet demands for currency it would jeopardize public confidence and might lead to runs on banks and to hoarding of currency, such as occurred in 1931.

It is already within the System's power to invoke such drastic measures. The System has rejected such a course because of the possible disastrous effects on the entire financial situation of the country. The proposal would appear to be designed to force the Federal Reserve System to abandon support of the Government securities market and thus bring about sharp increases in interest rates. It is inconceivable that Congress or the public desire either to create a run on the currency or collapse of the bond market. If that were the will of the majority, it should be done openly and frankly and not by indirection.

EXCESS GOLD CERTIFICATE RESERVES OVER REQUIREMENTS
OF 35 PER CENT GOLD CERTIFICATES AGAINST
DEPOSITS AND 40 PER CENT AGAINST FEDERAL RESERVE NOTES
July 31, 1948

(In thousands of dollars)

	Total required reserves <u>(35% and 40%)</u>	Excess of gold certificate reserves <u>reserves</u>
Boston	894,530	-16,063
New York	4,550,294	2,534,050
Philadelphia	997,087	75,232
Cleveland	1,362,301	152,012
Richmond	960,567	112,849
Atlanta	830,445	243,526
Chicago	2,889,077	1,521,868
St. Louis	699,706	-60,623
Minneapolis	439,810	51,992
Kansas City	708,449	154,123
Dallas	579,575	-1,472
San Francisco	<u>1,777,952</u>	<u>949,514</u>
Total	16,689,793	5,717,008

8/3/48

ACTUAL RESERVES NECESSARY ALLOWING A 3 PER CENT OPERATING MARGIN
OVER 35 PER CENT AND 40 PER CENT GOLD CERTIFICATE RESERVE
REQUIREMENTS AGAINST DEPOSITS AND NOTES, RESPECTIVELY
July 31, 1948

(In thousands of dollars)

	<u>Total reserves necessary including 3% margin (38% and 43%)</u>	<u>Excess of gold certificates available for purchase of Government securities</u>	
Boston	965,105	-86,638	
New York	4,916,822	2,167,522	
Philadelphia	1,075,579	-3,260	
Cleveland	1,470,104	44,209	
Richmond	1,036,018	37,398	
Atlanta	896,007	177,964	
Chicago	3,117,252	1,293,693	
St. Louis	755,050	-115,967	
Minneapolis	474,885	16,917	
Kansas City	765,206	97,366	
Dallas	626,667	-48,564	
San Francisco	<u>1,919,777</u>	<u>807,689</u>	
Total	18,018,472	4,642,758	total of positive figures

8/3/48