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May 25, 1933.

Dear Mr. Case:

Following our conversation of the other day I have been giving some further thought to the question of open market dealings in bankers acceptances. With their holdings of Government securities practically liquidated, and perhaps completely liquidated by the end of the next month, the Federal Reserve Banks will have practically no investments except their holdings of discounted paper and the bankers acceptances bought in the open market. Under present conditions, and with a discount rate that is generally below the market rate, the Federal Reserve Banks are not in a position to exercise much control over the market through the discount rate, and in the absence of some increase in the discount rate it is therefore particularly important, it seems to me, that dealings in bankers acceptances be governed by money and credit conditions. This it is difficult to do if the Federal Reserve Banks still adhere to the one-sided policy which has heretofore been followed with respect to bankers acceptances. Up to date the policy has clearly been quite consistently to buy but never to sell acceptances, and at all times to nurse the market for acceptances rather than to let it stand on its own feet, and for this there may have been some excuse in the beginning when bankers acceptances were new and had not been developed, but even before now there have been occasions, it seems

to me, when purchases of bankers acceptances have gone to uncalled for lengths and have led to dangerous inflation of credit. As you have said, the buying of acceptances by Federal Reserve Banks, particularly from the larger city banks, is but another form of discounting by commercial banks, and since the buying rate for acceptances is normally lower than the discount rate these purchases of acceptances need to be brought very definitely into harmony with the general credit policy of the Federal Reserve System, if the system is to maintain any effective relation to the credit structure. Even from the point of view of the development of the acceptance market itself I believe there is everything to be said for letting acceptances stand more and more on their own merits, without artificial support from the Federal Reserve Banks, and that this is particularly necessary if the Federal Reserve Banks, as it seems to me they must do, are to use their dealings in acceptances to give themselves more effective relation to the credit situation. To be more specific, this will mean, I should say, that the Federal Reserve Banks will have to recognise more and more that bankers acceptances, like short-term Government securities, must yield a rate that will be attractive to the market and should not be bought, and cannot be sold, at an artificially low rate. It must also involve a willingness on the part of the Federal Reserve Banks to sell bankers acceptances to the market as well as to buy them. Granted an independent outside market for acceptances, it seems to me that the Federal Reserve Banks ought to be able, through their purchases and sales to the

(Signed) S. P. Gilbert, Jr.
Under Secretary.

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market, to establish an effective relation with the money market
WASHINGTON
that under present conditions it is difficult to secure through the
discount rate.

May 25, 1933.
Very truly yours,

My dear Governor:

(Signed) S. P. Gilbert, Jr.

I am enclosing for your information a copy of a letter
of this date which I have sent to Deputy
Federal Reserve Bank of New York on the general subject of deal-

J. H. Case, Esq.,
c/o Federal Reserve Bank,
15 Nassau Street,
New York, N. Y.
subject was discussed at the recent meeting of
the Committee of Governors on Open Market Operations and I have
written Mr. Case in accordance with his request for an indication
of the Treasury's views as to what policy should be followed in
these operations.

Very truly yours,

S. P. GILBERT, Jr.,
Under Secretary.

Hon. D. R. Crissinger,
Governor, Federal Reserve Board,
Washington, D. C.

1 enclosure.