



Twenty-Seventh

ANNUAL REPORT

of the

**BOARD OF GOVERNORS *of the*
FEDERAL RESERVE SYSTEM**



**COVERING OPERATIONS FOR
THE YEAR**

1940



actions for the System open market account (including purchases, sales, exchanges, replacement of maturing securities, and letting maturities run off without replacement) as in its judgment from time to time may be necessary for the purpose of exercising an influence toward maintaining orderly market conditions; provided that the aggregate amount of securities held in the account at the close of this date shall not be increased nor decreased by more than \$500,000,000."

The action of the Committee renewed the authority granted to the executive committee at the meeting of the Federal Open Market Committee on March 20, 1940, and was taken for substantially the same reasons, with the understanding that the executive committee would have authority under the resolution to direct the sale of securities, within the limits fixed by the full Committee, not only for the purpose of exercising an influence toward orderly conditions in the market but also for the purpose of disposing of securities, which had been acquired in a period of market weakness, whenever there was a strong buying market and there were not sufficient offerings from other sources to meet demands.

The reason for this was that experience had indicated that the System ordinarily would be called upon to buy more securities during a period of market weakness than it would have occasion to sell during a period of rising prices for the purpose of exercising an influence of a stabilizing character, and, therefore, the Committee believed that securities which had been acquired during a period of market weakness should be sold whenever that could be done without adverse effects on the market.

MEETING ON SEPTEMBER 27, 1940

Members present: Mr. Harrison, Vice Chairman; Mr. Szymczak, Mr. McKee, Mr. Ransom, Mr. Davis, Mr. Draper, Mr. Sinclair, Mr. Parker, Mr. Schaller, Mr. Day.

Upon motion duly made and seconded, the following resolution was adopted, Messrs. Harrison, Szymczak, McKee, Ransom, Davis, Sinclair, Parker, Schaller and Day voting "aye," and Mr. Draper voting "no":

"That the executive committee be directed until otherwise directed by the Federal Open Market Committee to arrange for such transactions for the System open market account (including purchases, sales, exchanges, replacement of maturing securities, and letting maturities run off without replacement) as in its judgment from time to time may be advisable in the light of existing conditions; provided that the aggregate amount of securities held in the account at the close of this date shall not be increased nor decreased by more than \$500,000,000."

By this action the Committee changed the form of the existing resolution by substituting the phrase "advisable in the light of existing conditions" for the phrase "necessary for the purpose of exercising an influence toward maintaining orderly market conditions." This was done for the purpose of bringing the resolution more closely into conformity with the existing understanding of the authority conferred upon the executive committee as stated in the record in connection with the action taken on May 28, 1940. It was the opinion of the full Committee that the resolution should be in such form as to enable the executive committee to continue to direct the execution of transactions in the account not only for the purpose of exercising an influence toward maintaining orderly market conditions but also, within the stated limit, for the purpose of selling

securities which had been acquired during a period of market weakness, whenever such sales could be made without adversely affecting the market.

Mr. Draper voted against the adoption of the resolution for the reason that the changed instructions to the executive committee might be construed by the public as a change in policy having deflationary implications. He also felt that caution was particularly necessary at this time not only because of the domestic situation but also because of the dangerous war conditions abroad.

MEETING ON DECEMBER 18, 1940

Member present: Mr. Eccles, Chairman; Mr. Harrison, Vice Chairman; Mr. Szymczak, Mr. McKee, Mr. Ransom, Mr. Davis, Mr. Draper, Mr. Sinclair, Mr. Parker, Mr. Schaller, Mr. Day.

Upon motion duly made and seconded, the following resolution was adopted, Messrs. Eccles, Harrison, Szymczak, McKee, Ransom, Davis, Sinclair, Parker, Schaller, and Day voting "aye," and Mr. Draper voting "no":

"That the executive committee be directed until otherwise directed by the Federal Open Market Committee to arrange for such transactions for the System open market account (including purchases, sales, exchanges, replacement of maturing securities, and letting maturities run off without replacement) as in its judgment from time to time may be advisable in the light of existing conditions; provided that the aggregate amount of securities held in the account at the close of this date shall not be increased or decreased by more than \$200,000,000."

The above resolution was in the same form as that adopted at the meeting on September 27, 1940, except that it reduced from \$500,000,000 to \$200,000,000 the amount by which the aggregate amount of securities held in the System account could be increased or decreased. The reason for the action was that, because of the many uncertainties in the then existing situation which could not be appraised satisfactorily, it was believed that the executive committee should continue to be in a position to act in accordance with its best judgment within the limits of the resolution and in the light of developments from time to time, especially when it might be deemed desirable to exercise an influence toward preventing disorderly conditions in the market during the interval before another meeting of the full Committee, but that, in view of the large reduction in the portfolio that had been accomplished during the past several months, there was no need at this time for making further sales for the sole purpose of reducing the account.

Mr. Draper stated that he voted "no" on the above resolution for the following reasons which were broader in scope than those outlined by him when voting in the negative on a similar resolution adopted at the meeting of the Federal Open Market Committee on September 27, 1940:

"I do not believe that in the present circumstances sales from the portfolio are necessary in order to maintain orderly market conditions. I have seen no recent evidence of the market being disorderly. In my judgment, also, sales from the portfolio for the purpose of maintaining an orderly market should be resorted to much less frequently and less vigorously than purchases at a time when the market is declining rapidly. Rapid declines are apt to result in a selling wave amounting to panic, which I believe should be prevented when possible. On the other hand, there is little danger of a panic when

the market advances, and it makes little difference whether a rise is rapid or slow, so long as the level it reaches is appropriate to existing conditions and is not the result of purely speculative purchases.

“A still more important reason for my belief that there is no occasion to sell is that our portfolio has been reduced very substantially and that we shall need all the ammunition we can muster when reserve requirements will have been increased and the time comes to adopt a policy of credit restriction in order to prevent inflation.”