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TENTATIVE DRAFT - SUBJECT TO CHANGE

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Final minutes
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see letter
3/11/36*

MINUTES OF THE MEETING OF THE
FEDERAL OPEN MARKET COMMITTEE
HELD AT WASHINGTON, D. C.
JANUARY 21, 1936

The meeting was called to order at 10:45 a. m. The following were present:

Governor Harrison, chairman, Governors Young, Norris, Fleming, Seay, Newton, Schaller, Martin, Geery, Hamilton, McKinney, and Calkins, and Deputy Governor Burgess, secretary.

Governor Harrison indicated that the meeting was held at its own call in accordance with the unanimous vote of the meeting on December 17 to 18. Governor Harrison said he understood that due to the imminence of a change in the membership in the Board of Governors of the Federal Reserve System the present Board was not in a favorable position now to carry through any action recommended, but that fact he said did not absolve the committee from considering and expressing its views upon important questions of policy. These views would at least be available to the new Board as soon as organized even if the present Board should take no action.

On motion the secretary's report of operations and the preliminary memorandum were accepted and ordered filed, and the actions of the executive committee since the last meeting were ratified.

The secretary read a letter from the Board of Governors of January 20 with respect to one of the resolutions adopted by the committee at its meeting on December 17 and 18.

There ensued a general discussion with respect to the points of view which had been expressed, both inside and outside the Reserve System concerning various proposals for dealing with excess reserves. In the course of this discussion it was brought out that the situation had been somewhat altered by the new budgetary proposals, and the effect on the budget of Supreme Court action with respect to the A. A. A. and the possible passage of a bonus bill.

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During this discussion Governor Young left the meeting.

The committee discussed various methods by which, if it was thought advisable, the relationship between Federal reserve policy and fiscal policy might be recorded and possibly presented to the Administration.

[There was also a discussion of the question raised at the meeting of the executive committee on January 3, whether an increase in Treasury balances in the Reserve banks should be used as a method of reducing the volume of excess reserves. There was general agreement that this was not an effective and suitable method of dealing with excess reserves since its results could only be temporary and would be too limited in amount, and its use would involve complications because of possible conflicts of interest between the Treasury and the Reserve System.]

There was further discussion of the relation of the budget to Federal Reserve action during the course of which Governor Harrison read paragraphs from the President's budget message of December 29 and his Atlanta speech of November 29, both of which appeared to justify the impression generally held by the committee at its last meeting, that a tapering off of the deficit was probable.

Governor Norris presented for discussion, and to ascertain the general sense of the meeting a tentative draft of a resolution as follows:

[RESOLVED, that until further action by this Committee, or by the new Open Market Committee which will succeed it on March 1st, the System follow the policy of investing the proceeds of maturing Treasury Bills in Treasury Notes, having a maturity of three to five years, to such an extent as will yield approximately the same return in interest.

Further, that a public statement be made that this policy will effect a gradual reduction in the System's total holdings of Government securities, but that this reduction will be entirely in Treasury Bills, and that there will be an actual increase in the holdings of longer-term securities.]

[In discussing this resolution, Governor Norris stated that a primary consideration should be the proper administration of the Federal Reserve System.

The System to offset current maturities in the System account was now buying

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Treasury Bills it did not want at practically no yield. Under the resolution it would be necessary to purchase about one dollar of notes for every ten dollars of bills which were allowed to mature. In this way the longer-term government market would be supported, and the action would probably not influence rates beyond the Treasury bill market. Governor Norris indicated that he would not want to offer the resolution formally until after it had been ascertained that the Treasury Department would interpose no objection to the procedure indicated.

In the course of a general discussion Governor Seay pointed out that Governor Norris's proposal would go a very short distance in diminishing excess reserves.

Governor Harrison raised the question whether the suggested resolution would not be confusing when considered in relation to the December recommendations, as the two resolutions might appear to be contradictory or to represent a change of views.

Governor Calkins indicated the belief that any reduction in the holdings of government securities by the Reserve System would have large effects, in view of probable increased Government borrowing, and the risk involved in action of this sort would be greater than in December.

Governor Martin then offered the following resolution:

RESOLVED that certainty of recovery has not developed to such a point that action by this committee might not be detrimental. Therefore no action is the proper action at the present time, but that the situation should be again reviewed about the middle of February.

In the course of the discussion of this resolution it was pointed out that it would not be consistent with the December resolution. The resolution was not seconded.

There was then an informal discussion of proposals for a resolution which should have the effect of reaffirming the resolution adopted at the meeting in December, and Governor Calkins indicated he was prepared to offer such a resolution

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subject to detailed wording. A rough draft resolution was read by the Chairman.

The meeting adjourned at 12:45 to reconvene at 2 p. m. with the understanding that in the meantime the proposed resolution would be put into more finished form.

The meeting reconvened at 2:00 p. m. with the same attendance except that Governor Young and Governor Seay entered the meeting shortly after it had convened. The following draft resolution was then read:

(This draft includes a few later minor changes)

The Committee has considered the preliminary memorandum and has reviewed the credit situation. It is the sense of the Committee that, so far as business, credit, and banking conditions are concerned, there is nothing in the present situation to prompt the Committee to change its views as expressed in its resolution adopted on December 18, which the Committee respectfully renews.

The Committee recognizes that the risks of action are somewhat increased by the present budgetary situation, but it recognizes also that the longer action is delayed, the greater are the dangers resulting from the combination of inordinately large excess reserves and an unbalanced budgetary position, and the greater will be the difficulty of taking remedial action.

Viewing the situation as a whole, the Committee strongly believes that action looking toward a substantial reduction in excess reserves should be taken as soon as this may be feasible, in the judgment of the Board of Governors of the Federal Reserve System, having in mind the advantages of a coordinated program of recovery.

An informal expression of view indicated that a majority of those present were favorable to the resolution.

After discussion it was agreed that authority voted to the executive committee of the Federal Open Market Committee at three previous meetings to make shifts of maturities in the System open market account, should be continued as necessary in the proper administration of the account to enable the executive committee to replace maturities from time to time and to make shifts in maturities to meet changing market conditions. With respect to the amount of authority which the committee should have in shifting from shorter maturities to bonds, it was agreed that some limited authority was advisable in order to deal with any market

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situation that might arise. It was therefore unanimously

VOTED that superseding previous authorizations, the executive committee be authorized to make shifts between maturities of government securities up to \$300,000,000, provided that the amount of securities maturing within two years be maintained at not less than \$1,000,000,000 and that the amount of bonds be not over \$300,000,000.

It was also agreed that authority should be given to the executive committee to buy or sell (which would include authority to allow maturities to run off) securities for System account within limits as to amount, in order that the committee might be in a position to act promptly if circumstances not now foreseen should make action appear desirable before a further meeting of the full committee. It was therefore unanimously

VOTED that the executive committee be authorized to buy or sell up to \$250,000,000 of government securities, subject to telegraphic approval of a majority of the Federal Open Market Committee and the approval of the Board of Governors of the Federal Reserve System.

These motions would continue in effect similar authority voted at the meeting of the committee on December 17-18, 1935.

The question of another meeting of the committee was discussed, and in view of the uncertainties with respect to System organization it was agreed that adjournment should be sine die.

At 2:35 Governor Eccles entered the meeting.

Governor Harrison showed him the resolution which had been proposed, and Governor Eccles stated that he saw no reason why the resolution should not be voted on and indicated that the question of dealing with excess reserves was probably more a problem for the future when the new Board will have been organized.

Governor Harrison stated the view that if it were felt that banking and credit conditions indicated the need for System action, but that this action was hindered by other elements in the government program, it was at least the duty of the System to present the case to the Administration in some appropriate manner.

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At 2:35 Governor Eccles entered the meeting.

Governor Harrison showed him the resolution which had been proposed, and Governor Eccles stated that he saw no objection to it, but indicated that the question of dealing with excess reserves was probably more a problem for the future when the new Board will have been organized.

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Governor Harrison inquired about the results of the questionnaire relative to excess reserves which had been sent by the Board of Governors to each Federal Reserve Bank on December 19 and Governor Eccles indicated that he would send copies of the compilation of the replies to the members of the committee.

Governor Eccles left the meeting at this point.

Governor Harrison explained that the New York bank had forwarded to the Federal Reserve Board a study of the investment position of member banks in the Second District with the suggestion that the same sort of analysis might be interesting on a countrywide basis. Governor Eccles had suggested that copies of the study might well be distributed to the other Reserve Banks. As those present indicated an interest in the study, copies of the memorandum embodying it were then distributed. A copy of this memorandum is attached to these minutes.

The resolution on page 4 was then passed by the following vote:

<u>Yes</u>	<u>No</u>
Governors Harrison Norris Fleming Seay Schaller Geery Hamilton McKinney Calkins	Governors Young Newton Martin

Governor Martin explained that his negative vote was based on the belief that the facts do not yet show clearly that business has recovered sufficiently to make it wise to take action of this sort.

Governor Eccles re-entered the meeting at this point and discussed briefly the question of excess reserves. [During the course of this discussion he pointed out that he did not yet feel seriously concerned about the effect of excess reserves, since there had as yet been no excessive credit expansion; expansion was in fact desirable in the mortgage field and in the capital goods industries as a means of putting people to work.] The better the terms under which

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money could be afforded, the greater the probability of its use. A wider use of money in these directions would tend to solve the budget problem, he said.)

It was his view that the only danger lay in the difficulty of preventing the excessive use of funds for speculative purposes, for the bidding up of prices of existing properties, rather than for increased employment. He indicated, however, that this problem could be dealt with in part at least by regulations with respect to the use of credit for carrying securities. Too long a delay, however, in dealings with excess reserve would mean that when action was taken it could only take the form of a reversal of policy, and when this took place there would be more banks which had used excess reserves so fully that they would be vulnerable when reserve requirements were finally increased. He raised the question whether the policy could not be adopted of preventing further accumulation of excess reserves beyond \$3,000,000,000. If that were done, then a decrease of a billion dollars at any time would bring the volume of excess reserves within range of flexible operations in the open market.

In the course of general discussion Governor Harrison raised the question whether action which might be taken to reduce excess reserves through an increase of reserve requirements should not perhaps be accompanied by a reduction of discount rates as an indication that the System was not in fact desirous of restraining the use of credit but rather desired without reversing its easy money policy to correct a situation now fraught with possible dangers.

Governor Eccles raised the question whether it might not be desirable at the same time to make an announcement that the Reserve System would loan at par on government bonds.

┌ Governor Harrison raised the question whether there needed to be any public statement following this meeting of the committee, and it was agreed by Governor Eccles and the governors present that it would be desirable to have no public statement. ┘

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There then ensued an informal discussion with respect to the organization of the new open market committee, during the course of which a majority of those present indicated informally that they believed the alternate provided by the law should be from a different Reserve Bank from that of the member of the committee.

The meeting adjourned at 3:40 p. m.

W. Randolph Burgess,
Secretary.