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RESERVE BOARD FILE

333.1

Mr Herron 12/19/24

MEETING OF THE OPEN MARKET INVESTMENT COMMITTEE FOR THE FEDERAL RESERVE SYSTEM WITH THE FEDERAL RESERVE BOARD, HELD IN WASHINGTON ON FRIDAY DECEMBER 19, 1924.

333-b-2

Final minutes 12/19/24

PRESENT: Messrs. Crissinger, Platt, Hamlin, Miller, James, Cunningham.
(Members of the Federal Reserve Board.)
Hon. G. R. Winston, Under Secretary of the Treasury
Hon. J. W. McIntosh, Comptroller of the Currency
Messrs. Strong, Harding, Fancher, McDougal and Norris.
(Members of the Open Market Investment Committee.)
Mr. Hatteson (Secretary of the Committee.

Governor Crissinger called the meeting to order at 10:30 a.m.

Governor Strong then presented written reports by himself as Chairman of the Committee and by the Secretary of the Committee.

Governor Strong: - I dislike to ask the members of the meeting to read all of these documents and figures on such short notice, but they were prepared at the last minute. Briefly, what has happened is this - we had two matters to deal with in connection with the Committee's account. To see that intended subscribers for the new 4% Treasury loan who wish to pay with March certificates and notes were given an opportunity to get them. The market was bare of them and we supplied the market freely from a 2% basis down to one transaction on a 1% basis liquidating in round figures about $85,000,000 of our holdings of the March maturities, in order to enable subscribers to take the 4% bonds. I think everything we sold for our own account and for the Treasury was immediately used for subscriptions. The effect of that would have been, had we regarded these as final sales, to take a very large amount of money out of the market, plus the December 15th maturities, so as soon as we sold the March maturities they were replaced with other maturities. We were successful in replacing all but about $17,000,000. The market became bare of things we could buy maturing in 1925. We had arranged with the Treasury to anticipate $30,000,000 of our December holdings and the other $35,000,000 run off

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on December 15th. The net result of the transactions which we have had has been to replace $15,000,000 of the $65,000,000 which matured on December 15th, the other $50,000,000 being allowed to run off. The arrangement from day to day was governed by what was going on in the money market and in connection with subscriptions, and the net result has been to reduce our government holdings by $50,000,000, without any appreciable effect on the money market. One day the rate was 4% and yesterday it was 3¼%, but we think there is a possibility of a little tighter money because the rate on time loans has gone up to 4% for loans maturing in the Spring and that is a pretty good indication of the feeling of the Street about money. Our program has worked out exactly as we thought, with the exception that we have not replaced as much of the December 15th maturity as we thought might be necessary. We have made a very large turn over for the Treasury in connection with these transactions. [The Committee feels that from now on the account should not be increased above what it is and that we should liquidate small amounts of securities. At the Bank in New York there is a feeling that it would be a very good thing if the borrowing we anticipate should take place now would be in the form of discounts and when the return of funds takes place after January 1st, the discounts will be a buffer, along with bills and securities, to absorb that money. If there is any excess money after January 1st, I would advocate marketing a small part of our investment account.]

[Governor McDougal: - In endorsing all that Governor Strong has said, I feel very strongly that unless something unexpected should happen the trend of our holdings in the special account should be downward. I do not see any reason at the present time why there should be great activity on the part of this Committee. Personally, I would like very soon to see this activity decreased and let the money market find its own level. My impression is that after we had re-

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duced gradually our holdings of securities to $250,000,000 or $300,000,000, or even $200,000,000, we would still probably have a stock in hand large enough to exercise what influence may be necessary from time to time. We have gone far enough now to determine what amount we should have on hand.

Governor Strong: - I do not think we have had enough experience yet. I hope the members of the Board realize that as a result of all transactions of the Committee, the earning assets of the System have in fact been reduced, although they temporarily look as though they have been increased because of temporary borrowings in New York by the Treasury.- With those borrowings liquidated you will find a reduction.

Mr. Hinton: - The Treasury has repaid all of these temporary advances.

Governor Strong: - I think that to have our investment account reduced $50,000,000 and our actual discounts decreased, is the best evidence in the world that the influence of these transactions has been favorable to our policy in spite of the fact that there were pretty heavy borrowings in Chicago and Cleveland yesterday and the day before.

Governor McDougal: - Our borrowings were somewhat increased and I expected more yesterday but have no figures. There is not much loose money in Chicago now but I should think our banks would first go to New York because they have a large amount of money there at the present time.

Governor Strong: - I do not think you can tell until tonight what the result is because the Treasury will take $70,000,000 out of the Federal Reserve banks and other depositaries to make its payments and that may induce some further borrowing. We anticipate that may happen and we are expecting to find it necessary to advance our bill rate to 3%. That will be the last advance we can make. We will then have a flat rate of 3% on both bills and discounts.

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Mr. Winston: - We had more cash payments for our bonds than we expected. Taxes have come in faster this month and the Treasury will leave a little more money in the Federal Reserve banks.

Mr. Platt: - Doesn't the increased revenue from activity in the stock market mean anything?

Mr. Winston: - Not enough to be felt. Our overdraft on Monday was $143,000,000; on Tuesday, $75,000,000; on Wednesday, $40,000,000; and on Thursday about $10,000,000.

Mr. McDougal: - The commercial paper rate has advanced at least one quarter. It is 3½% to 4% now.

Mr. Platt: - I do not think the rediscount rate should be more than one-half percent below the commercial paper rate.

Governor Strong: - Mr. Platt, do you think the New York banks would pay 3% on deposits today?

Mr. Platt: - No.

Governor Strong: - Then why should they pay us 3% on discounts which is the same thing?

Mr. Platt: - They are doing it now. The discounts of your large banks make a very large proportion of your present borrowings.

Governor Strong: - Our country banks have the most now but that is only $20,000,000 or $30,000,000. The New York City banks with the money market as it is, pay us off the minute they can do so and they do it by calling stock exchange loans. They do not want to be paying us 3%. They figure the cost of our money plus the overhead and find that this 3% money costs them about 4%, and evidence that they are not borrowing from us is that they pay off the minute they can. The total borrowings in our district are about $53,000,000. Do you

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advocate advancing our discount rate?

Mr. Platt: - I think it is pretty low, but would not recommend just now that your directors increase it, but after the first of the year I would advocate it pretty strongly. It seems to me that if Chicago can get along with a 4% rate, New York should get along with 3½%. I am inclined to think any way that city banks should not borrow from the Federal Reserve Bank but should get accomodation through acceptances. Then the rate could be fixed with relation to country banks.

Governor Strong: - I gather from this that you would increase our rate to 4% or 5%. If we made our rates with relation to our country banks upstate, we would have a 5% rate all the time. We deal with these banks by personal contact. When we find they are abusing us we get after them. We found that the borrowings of one bank were going up in order that it could put some money out in its community at 4%. We got after them and stopped it.

Mr. Platt: - I think after January 1st I would increase the rate to 3½%.

Governor Harding: - Ordinarily money in the big centers is cheaper in January than in December, on account of the return flow after Christmas.

Governor Strong: - Would you advance the discount rate when we have $450,000,000 of investments in the System?

Mr. Platt: - I would run some of them off and test the market out.

Governor Strong: - That is what we have in mind, and that is how we approach the discount rate question.

Mr. Platt: - The first thing to do is to get the bill rate up to 3%.

Governor Strong: - We will probably do that the first of next week. We have it in mind.

Governor Crissinger: - Governor Harding, have you any remarks that you would like to make?

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Governor Harding: - I think that the Federal reserve banks should have on hand at all times a certain amount of Government securities; just what amount I am not prepared to say. Maybe the amount we have had is too high, but we should have a certain amount of them so as to be able to revert market conditions without interfering with rates. Perhaps experience later will tell us what the amount is. As regards the rate, it seems to me that as far as large banks are concerned, the bill rate is the important factor. This is made primarily in the open market, but the action of the Federal reserve banks in buying bills has had a great deal to do with the stabilizing of the bill rate. These bills are offered to the Federal reserve banks both by brokers and by banks. In Boston where our discount rate is 3½%, we have passed through such seasonal activity as we have had without any direct borrowing on the part of any large member banks. Our total loans are about $18,000,000, mostly for country banks. The large banks as they need money are buying clearing house funds. Some concerns in Boston deal in these funds. If a bank has a debit it offers to buy clearing house funds at a rate below the discount rate and sometimes below the bill rate. If the Federal reserve banks should now hold off from the bill market, in my opinion it would only be a few days before banks would offer bills at 3% or go to New York at 3%. I think we have a good secondary control of the money market in the rate at which we buy bills. As far as we buy at the current rates, we tend to keep the market easy. I think Federal reserve banks should always be in the market at a rate. A very active bill market has developed in Boston in the last sixty days.

Governor Fancher: - There is probably a very substantial volume of bills in the market. I think there are several of the larger banks accepting pretty well up to the limit, indicating a substantial volume of bills.

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Governor Harding: - One large bank in Chicago recently complained of abuse in the acceptance of domestic bills and said that they were obliged to make acceptances. The other day among some bills we had bought I noticed some were accepted by this very bank.

Governor McDougal: - I think I could pick out that bank. It was suggested to me that we should be very careful, but I told that man that the responsibility was his and that we depended upon him to see that the underlying transactions were in accord with the spirit and letter of the law.

Governor Fancher: - We have had certain correspondence with the Federal Reserve Bank of Chicago about certain bills of that bank.

Governor Harding: - The Federal Reserve Act didn't originally provide for domestic acceptances. Some years afterwards a clause was put in that acceptances might be made against goods in transit and the Board's regulations indicated that the normal time in transit should be taken into account. Later regulations have opened the door a little so that now commodities are put in warehouses, receipts issued and acceptances run as long as ninety days.

Governor Strong: - This committee has a job on its hands. We spent two days in New York going over the situation and our operations together. I think the committee knows all about it that I do and the net result is a very simple thing. We have reduced our account $50,000,000 and the earning assets of the System have not increased. The question is the policy to be pursued from now on.

Governor Crissinger: - Does any member of the Board wish to speak?

Mr. Miller: - I have my individual views but I suppose Governor Strong wants to know what the Board as a whole thinks.

Governor Crissinger: - I believe Governor Strong would like to have the comments of the different members.

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Governor Strong: - That is right.

Mr. Miller: - I look at it all as a question of the adjustment of Federal reserve rates to the trend of the market. At the present time the commercial paper rate is 3½% or 4% and the acceptance rate, according to this report sent to the Board, is 3% to 3 1/8%, except on long maturities.

Governor Strong: - That is what dealers bid for unendorsed bills. The bills we buy are endorsed and the rate is at least one-eighth less.

Mr. Miller: - That would make the acceptance rate 2 7/8 to 3%. The maximum Federal reserve rate thus far has been 2 3/4%, so that we are under the market even with the advances that have taken place in the last two or three weeks. There arises in my mind a question as to how far it is desirable to go into the new year without a rate that is equal to the market or a little ahead. The Federal reserve banks' assets have gone up $300,000,000 from the low of the year. The great bulk of the increase has been in acceptances. Since August 1, we have purchased over $300,000,000 of acceptances. As far as our rates go, the only important rate is the buying rate on acceptances. With that rate below the market rate, even though no more than one-eighth or one-fourth, I feel there is a real question as to how long we ought to go along without an increase.

Governor Strong: - We are proposing to advance the rate to 3%.

Mr. Miller: - The market may go one-eighth ahead of it then. My thought is that until we have a clearer basis on which to prognosticate a clear policy in the year 1935, until we have warrant for believing we are not going to have a considerable advance in industry, it is taking some risk to maintain a rate that virtually makes the acceptance rate. I would feel more comfortable if we increased the rate to a point where acceptances would not come to the reserve bank. Our responsibility is still greater if we are holding down the accept-

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ance rate to an artificial level in order to avoid the necessity of raising our rediscount rate. We are really proclaiming an artificial market.

Governor Strong: Would you tell me what you would do if you were in New York?

Mr. Miller: I would advance the buying rate for acceptances to a point that would keep acceptances from coming into the reserve bank. I would advance it until it was demonstrated, by actual applications for rediscounts, that the market was dependent for accommodation upon the Federal reserve banks, and that the member banks felt this dependence so strongly that they would actually come in and rediscount.

Governor Strong: They are demonstrating that dependence in what they are doing - selling bills with their endorsement at a rate of 2 ⅝ per cent.

Mr. Miller: The acceptance rate, for practical purposes, is a rediscount rate but it is not an effective rate. In the situation we are in now, which is subject to different construction - it may be we are going to have a very temporate movement of business, maybe a very active one - I think it is not desirable to predicate our policy on either extreme view but it is very desirable to feel out the market, and I regard the acceptance purchases and sales as a method of finding the range. As long as the Reserve System maintains a buying rate that attracts acceptances, it makes the acceptance rate. How far the rate would have to be advanced to force the absorption of acceptances by the market, I do not know; nobody can tell at this time. I do think it would be a good policy, moderately conservative, just to take advantage of the general back-swing in January to edge in by advancing our rate on acceptances. I think we could tell by the middle of the month whether or not we are going to have a situation that

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would warrant an advance in the discount rate for any other reason than purely for appearance. If we went into February with easy conditions, I think the proper policy then might be to move the acceptance rate downward. But if not, and we moved into pretty heavy pressure in February, I think we should then be prepared to move the discount rate up, in proper relation to the trend of the market and the acceptance rate. At the present time I would move the buying rate up to 3 per cent; if I got acceptances at 3 per cent, I would put it up to 3 and 1/8 per cent. If that resulted in a growth of discounts I think we would have to take reckoning of what lay behind the demand for rediscounts. If it was just seasonal pressure I would not be greatly disturbed.

Governor Strong: We feel that is what is taking place. We always have liquidation after the first of the year. We figure we will have it this year, although perhaps not as great as usual.

Governor Fancher: With the buying rate on bills advanced, your rate will probably go to 2 ½ and 3 per cent.

Governor Strong: 3 per cent for everything except 30 days, leaving that at 2 ½ for a few days and then advancing it to 3.

Mr. Miller: When you are going to have a return flow, I think that is just when the rate can be made effective.

Governor Fancher: I think that from the 10th on through January we will be able to test this bill rate.

Mr. Miller: I think we have got to watch them very closely with regard to the discount rate. At the present time we are generally trying to operate without discount rate changes. That seems to make it more important that we should operate on some policy clearly related to the trend of the market. I am not

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afraid to face the possibility, that may at any moment turn into a probability, that the discount rate should be advanced. We have built up a technique under which we have a new implement and I think the buying rate on acceptances is the instrument with which we should work first. I would like to see that more closely adjusted to the movement of the money market. I am skeptical of any too loose artificial rate and can't get away from the impression that, however innocuous it may be in the present circumstances, we are taking a serious chance in maintaining our rate where it tends to keep the market rate down by a flow of Federal reserve credit into the pool. I anticipate that if we get an active movement of industry next year we will see a jump in rates that will give us all the shivers; and a pressure for reservebank funds that we will wonder where it is coming from. We have an enormous volume of credit pumped into the market, and member banks are going to be put to it to meet demands. They will go to the reserve banks to get it. We will be on the whole in a better position if we advance the rate now, instead of having the Federal reserve banks over a pretty long period of time, five to seven months, with very low rates, and then begin to move very rapidly forward, for if you do not move forward you would be taking the responsibility of adding in credit to the market of the country with the possibility of serious indigestion. I would not take a chance of making a mistake, when the alternative is the rather slight one of making the acceptance rate really effective by keeping acceptances out of the reserve banks and letting the market take care of its own, with the possibility that after January 1st we will discover borrowing taking place that indicates real pressure on the reserve banks and advance the discount rate. I am not so much concerned with what would

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happen then, as with what will happen if we ride along without a change.

Mr. Cunningham: You really feel that the rate should go to 3 per cent? They have agreed to do that, but you can't go over the rediscount rate. They are going to watch the situation. Let the committee go ahead with this thing. As near as I can learn, they are going to do the very thing you are trying to have them do, and I would let them alone. We can meet again in a short time. The situation I think will change after January 1st. I don't want at this time to raise the discount rate but I am ready to raise it when there is any necessity for it. The Committee is giving this serious consideration. I think from what they have reported here now, I am pretty clear as to what they are attempting to do and I want this committee to go on and perform their duties in accordance with their judgment. If their tendency is contrary to what we believe is proper, we have access to the committee at any time. We have got to give somebody our confidence and we should let the committee deal with the market from day to day. I don't want to enter any confusing element into the practices they are trying to carry out. I think the acceptance rate should go to 3 per cent, but I can't see where you could properly go above 3 per cent. I think you have got to let the situation reach its normal level some day.

Mr. Miller: On the supposition that a 3 per cent rate is maintained and acceptances still come into the reserve banks, would you let them come in any volume, say $100,000,000 in the course of three or four weeks?

Mr. Cunningham: I didn't say that definitely but I would trust the judgment of the committee in one adventure any way.

Governor Strong: The whole discussion seems to be based on the theory, with which I disagree, that we have an artificial money market. Banks would borrow from us now at any rate and if you wish to see all rates go up, all we have got

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to do is to keep advancing ours, because the market will keep ahead of us so long as the seasonal demand is on. We can charge any rate for this accommodation - 4 per cent or 5 per cent - they will still borrow from us.

Mr. Miller: How would you ascertain whether any rate at a reserve bank is artificial?

Governor Strong: The most artificial rate at the Federal reserve banks is so much above the market level that they don't use us at all. What we want is a rate at which banks are not too heavily penalized and which will not affect a contraction of business. If we put the rates up in the face of seasonal demand, we will do very much more than simply regulate borrowings. We will give the country a warning of a character that is going to do damage. I haven't found any business man in New York who has given me the slightest indication that there is anything in the business situation that indicates unsound speculation or stocking up of goods.

Mr. Miller: That was the most definite impression that I got when I was in New York last week.

Mr. Platt: What do you expect to see the dealers do when you raise the rate to 3 per cent.

Governor Strong: First they will develop a feeling of uneasiness, lest we should put the discount rate up. They will try to sell their bills as soon as they can and we hope at that level of rates they will succeed in distributing the bills. We expect that after January 1st rates will suddenly take a drop, the bills won't come in to us and the whole situation will be over.

Mr. Platt: Supposing the rate was raised above the discount rate?

Governor Strong: The banks would borrow from us at 3 per cent. Dealers are now carrying about $60,000,000 or $70,000,000 of bills. We were carrying their

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portfolios almost entirely and now they have practically paid us off. A very interesting thing to watch is the fact that the minute Federal reserve funds are quoted below the bill rate our bills go right out. We have had Federal reserve funds quoted below our rate in the street for the last two or three days and the result is our earning assets have not gone up. I have reports made up every hour which Mr. Case and I keep on our desks. On the 17th reserve funds were quoted at 2 - 2 ½ per cent. The minute this condition appears, we know that banks which have credit with us sell those funds for the day and the bidding for those funds is by banks or brokers who owe us money. That is the instrument by which they distribute surplus reserves. By watching the relation of what rate and the other rates we can tell what is going to happen to the surplus money.

(At this point Dr. Stewart entered the meeting)

Mr. Miller: I would like to have Dr. Stewart's explanation as to the economic significance of the growth of $365,000,000 in member banks' reserve deposits in the course of the year. What do you think that is due to and what does it indicate as regards the member banks' credit potentialities?

Dr. Stewart: From the middle of the year on there was a growth in acceptances and from July on an increase of $100,000,000 in securities purchased. Most of the increase occurred during the middle of the year.

Mr. Miller: All this is very largely accounted for by the purchase of acceptances in the past four or five months. We put money into the market and the market has put it into the member banks.

Dr. Stewart: I think it has been pretty well absorbed already in the growth of deposits of member banks. They have purchased investments and made loans on stocks and bonds.

Mr. Miller: The banks have been investing ordinary current demand deposit money, not in liquid commercial loans but in long term investments. They have

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been lending commercial money to the investment market and when the demand comes, there is going to be pressure somewhere.

Governor Norris: Has not that growth in investments been very largely the result of the great growth in time deposits as compared with the small growth in demand deposits?

Mr. Stewart: Time deposits have not increased during the last six months. Now, as I understand the Committee's report, the Committee regards it as undesirable to let surplus funds accumulate in New York, intends to raise the bill rate to 3 per cent, and that the period under consideration is between December 19th and January 10th.

Governor Strong: At this time banks are borrowing from us anyway. I expect that after January 1st there will develop a return flow of funds and some liquidation, and that then we must not let rates for money in the open market get too low. I would like to see the bills run off to some extent, reducing the earning assets. If that goes on indefinitely and we have easy money and there seems to be evidence of anything unsound, I would begin to liquidate some of our security holdings too. My feeling is that the bills will not mature fast enough to take up the return flow and that we will have to sell some securities too. I think after we put the bill rate up whatever demand is made upon us will be in the form of rediscounts and those borrowings will furnish the buffer for the first return. If that does not take place fast enough we will have to sell some securities.

Governor Norris: Governor McDougal, you think, aside from any necessity, that it is desirable that we should sell some securities?

Governor McDougal: Yes. When the question came up ten days ago as to the desirability of letting some March maturities run off, my view was in favor of it.

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$25,000,000 were mentioned and I said I would like to see them go just as far as the market would take them. I believe that we have gone far enough to know that $500,000,000 in that special fund would answer the purpose for which it was created; that is, putting us in position to exercise a stabilizing influence on the money market.

Mr. Miller: Not a stabilizing influence; I would call it a restraining influence on a market that is running ahead too rapidly, and I would, therefore, differ with you and say it was not desirable to liquidate if the evidence does not indicate that the situation calls for that. You want to sell them when the market does not want them but is obliged to take them because the reserve banks decide the market needs restraining. If we ever get in a position where we need these $500,000,000, in addition to the acceptances, I think it proves that they are really needed. The question in my mind concerns itself largely with what we may have to face in the late winter. I take it that Governor Strong is inclined to the view, which I think is a very rational view, that we should not run up the cost of credit until we have to, until we think some harm will result from cheap money, and in the interim pursue a stabilizing policy. I am rather disposed to hedge in this matter, probably because I am not concerned with the so-called chill that will come from an advance in our rate, nor am I disturbed over the Federal reserve banks appearing ridiculous by having their open market rate above the discount rate. As far as the Committee's immediate program is concerned, there is nothing that I have to take exception to. I think we have got now one of the most complicated situations that we have ever had. We do not know whether we are going into an easy winter next year, or whether business will show real momentum at that time.

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Governor Harding: If the object of having Government securities in the Federal reserve banks' portfolio is to exercise a restraining influence, we should not sell entirely out. I think we should always have some stock on hand; otherwise we can only exercise a restraining influence in one direction - we can only buy, we have nothing to sell.

Mr. Miller: You sell only as you need to sell in order to restrain. I would not sell for any other reason.

Governor Harding: We sold entirely out in March of 1923 and commenced buying again in December. Professor Sprague of the Harvard School of Business recently asked me to come before one of his classes. There are some pretty bright young men there, and Professor Sprague said some questions would be asked. I told him I would either answer the questions or evade them. One man asked if the Federal Reserve banks did not have $500,000,000 or $600,000,000 of Government securities in the spring of 1923 and said that when the Federal reserve banks sold out in 1923 the good times we had were just killed, and asked me how about it. I asked him if he remembered that the Federal reserve banks bought some securities in December, 1923 and in the spring of 1924, about $500,000,000, and why, if the action of the Federal reserve banks in selling out in 1923 killed business, did not the reverse action in 1924 create a boom.

Governor Norris: I would like to ask Governor Harding whether he considers that answering or evading the question.

Governor Crissinger: Now we would like to have Dr. Stewart make such comments as he desires with regard to the present situation.

Dr. Stewart: I think on the basis of facts for November there is a disposition to underrate the extent of the improvement in the business situation. The move-

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ment in the business situation has been so mild in comparison with the advance on the stock exchange that business men are inclined to minimize the increased business activity. The production index shows some further increase and there has been an advance in industry and a rise in prices, which has not been confined to agricultural products but has been shared in by most of the raw materials. There is a very considerable spread in the price rise among non-agricultural products. Increased activity in iron and steel has brought present production up to about 80 per cent of capacity and there is some disposition to order in advance of current needs. It seems to me that a very considerable thing has happened and that you have got to consider the question from the standpoint of what has happened and not what is expected.

Governor Strong: Do you believe the time has arrived to take any action which business interests could construe as a restraint on activity?

Mr. Stewart: It seems to me that there is a question of policy which remains unanswered, which is the desirability of disposing of government securities in January in order to give a different composition to our earning assets. I think there are certain general principles involved. The discounts are at such a low level and can be wiped out so easily, I cannot see how you can escape consideration of some further sales of government securities.

Governor Strong: Next January will present an opportunity for dealing with that question better than today. We can then sell some securities and put the market under a little pressure. I think we have a situation that requires watching and nobody can watch it closer than we are. What I want to draw out is whether anybody believes, with seasonal borrowing as it is, there is at present any need for selling our securities and forcing an advance in the discount rate. Personally, I do not think that is a desirable thing.

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Dr. Stewart: It seems that a policy which does not contemplate a change in the discount rate, when the Federal reserve bank is the largest factor in the market, gives you no standing to operate on.

Governor Strong: I know very well that we are going to advance our discount rate next year. I am not convinced yet, the way things are going, that it would be best to advance our discount rate. I think the turn of the year will disclose that but you must remember that we can kill business in this country very easily.

Dr. Stewart: Do you think an increase to 3 ½ per cent would kill business?

Governor Strong: I think at the moment it would have a very chilling effect.

Mr. Platt: Wouldn't genuine business take an advance in the very low rates we have been having as a mere indication of good business?

Governor Strong: I would not say that. I think it is going to be very much easier to advance the rate from 3 to 3 ½ per cent than it was to advance it last year from 4 to 4 ½ per cent. The way to get the rate advanced is just as Dr. Stewart has described - to liquidate the securities and establish a higher market rate and prepare the minds of the people for an increase in the discount rate. When we advanced the rate before, commercial paper was at 6 per cent.

Governor Norris: I think all our discussion has been interesting but I think it might be separated a little. This Committee which was appointed by the Board, at the last conference submitted certain recommendations having to do largely with the December 15th transactions. It has now submitted a report to the Board in which the story is told of what has been done to take care of the December 15th maturities and while the Chairman of the Committee has consulted constantly with the Committee, the initiative in everything has come from him and all the execution has been in New York, and I think it has been extremely well done and that large and difficult transactions have been handled without any trouble what-

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over. We hope that the report of what has been done has your approval. This report makes no recommendations. There is no request that the Board should adopt any resolution or give us any authority. The report has been supplemented by the statement of the Chairman that it is proposed to raise the bill rate to 3 per cent and that the return flow of funds in January could be taken care of by a further reduction in our security holdings and that the effects of this rate change on the money market and the effect of any sales should be noted before anything further is done. That is the general attitude of the Committee and the way it proposes to operate unless you object. I think we might understand that as far as we go we have your approval and that around the 10th or 15th of January we will review the situation with you and see what further steps should be taken within the few weeks or month after that. The question of the discount rate in New York is not a question for this Committee, except insofar as its operations might hasten or retard the time when that rate should be raised.

(Mr. Hamlin then moved that the Board note with approval the report of the Committee, including its proposed future action as contained in the statement of the Chairman. This motion was unanimously carried.)

Governor Strong: There is just one more possibility in the situation that has not been discussed and cannot be except from day to day. There are two things taking place in New York which possibly are a little unexpected. There has been a marking up of the time money rate to 4 per cent, which to my mind is an indication of two things; first, that brokers are getting a little nervous about the stock market and the possibility of further advances. After a broker sees customers coming in to buy day after day, he starts to get a little time money. Second, there is no tightening of the money market which we would normally expect immediately afterthe transactions of the Treasury. We loaned the Treasury

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$140,000,000 which was dumped into the market and we have liquidated $50,000,000 of our investments, but still there has been no increase in our earning assets and money yesterday was at 2 ½ per cent. If that situation continues I may wish to recommend to the Committee to sell some securities before January 1st. If Monday I find a good big surplus in the New York banks and we go over the Saturday statement with a surplus reserve, I am going to get in touch with some of the banks over the telephone. There may be borrowing in other districts that puts funds in New York.

Governor Fancher: Have you any estimate of how large an increase there has been in brokers loans in the last two or three weeks?

Governor Strong: Immediately after the election there was a small increase, then they went off again and they went off because the country came to New York to buy stocks largely for cash. In six houses which I consulted, there was only one which had not experienced a reduction in its loan account since the election and that was because of purchases by two wealthy men who bought securities but did not have cash enough to pay for them at the time.

Mr. Miller: I have noticed that there is a spirit of caution among business men, manufacturers and distributors. I noticed that Dun in his last weekly review emphasizes that point and it raises a question in my mind as to why it is. What is the cause of this caution against making commitments? I think it is a thing that is well worth considering, whatever the explanation may be. May it be due to the activity of the stock market or is it that business men are watching the growth in the volume of credit? Possibly the Federal Reserve System may be a factor in it. At any rate there are two things - one; we have this spirit of caution despite indications that we are going into a real forward move-

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ment of business, and two; how long can we count on that as an ally in restraining any undue expansion in credit.

Mr. Jones: It seems to me that the business men of the country watch rather carefully the trend of public opinion and public activity, and as I see it, the propaganda that has been going on, due largely to the wise leadership of the President, toward economy, is having a very desired effect upon the expenditures of individuals. There is a spirit of economy gradually growing throughout the country and the public is not rushing in to buy to the extent that was anticipated. That is reflected to my mind by the fact that retail stores are ~~not~~ NOW putting on sales that ordinarily are not put on until the middle of January. The retailers are finding themselves embarrassed by the fact that the public is not buying. Sales of gasoline indicate that the people are not joy-riding to the extent they were some time back. It seems to me that the program outlined by the President for Congress is having its effect on the general public, and to my mind that answers Mr. Miller's question. I think the American public is awakening to its folly. Another factor is that the business men throughout the South are scrutinizing their credits very much more carefully than they did under ordinary conditions, and are not extending long time sales of merchandise. The farmer is not rushing forward and signing on the dotted line as freely as was anticipated. He is conserving what he has and paying off his debts. That is reflected in increased deposits. There has been agood cotton crop and many debts have been liquidated out of that crop. They are not making commitments for 1933 very freely just now. My own industry is probably 33 1/3 per cent below what it was a year ago.

Dr. Stewart: What increased buying power there has been is very largely due to the continued foreign loans.

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Governor Strong: I would like to give you some information I have gotten from men I have talked with, like Mr. Grace, of the Bethlehem Steel Corporation, Mr. Murphy, John Ryan, Young, Woolley, Whitaurch and others. When I asked Mr. Murphy about the Christmas trade he said - "It is just about an average trade, pretty good, but we are bothered like the devil because nobody would order in advance and now we are getting telegrams for immediate shipments. They would not take the risk of buying ahead because they got stung so in 1920." Mr. Grace said the increase in the business of the Bethlehem Steel Corporation was distributed over every department of their business, with jobbers buying just a little ahead to take care of demands in the immediate future. They all say that the margin of profit is still very low. The thing that controls in this country is the mood of the people and it can be changed like a flash. The reason I don't want to see the discount rate changed now is because I think an advance in the rate will do harm. An advance in interest rates would do good and an advance in the discount rate in due course might do good. Let's be careful and pick the time. Mr. Alexander said that the only danger in the situation was that the Federal Reserve System would do something foolish about discount rates. He said every evidence in his bank was this very caution with which business is proceeding. If you change this caution into fright, it will do harm rather than good. That is my best judgment.

Mr. Jones: One of the most disturbing factors in the minds of business men in the condition of the overhead expense, due to gradual increasesin salaries, etc., to a point where the possible margin of profit is reduced to a minimum. There are very few concerns now that are not very seriously studying and wondering about conditions which exist at the present time. If they attempt to reduce salaries, they are in the position of losing the services of desirable men and reducing

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the morale of their institutions. I don't think there are any manufacturers or large merchants that are considering at the present time a reduction of what you would call mechanics' salaries. There is a feeling that the wage scale should be maintained but the question of overhead in the conduct of business is one which is receiving most careful consideration.

Governor Norris: If a man anticipates a profit of 20 per cent on his production, he is much more disposed to enlarge his business than on a 2 or 3 per cent margin.

Mr. Jones: Gradually advancing salaries and overhead has about brought you to a point where the margin of profit has been wiped out.

Mr. Miller: This margin is the difference between the buying and selling prices. Your margin of profit increases as the prices for which you sell rise.

Mr. James: Yes, but you must consider the cost of operating. Formerly, a 10 per cent margin gave a fair rate of return on your capital investment, but today a 13 per cent margin doesn't. The merchants of the country are gradually appreciating more and more the desirability of operating their businesses in a scientific rather than a speculative way. In my own business we used to think that a turnover twice a year was good. We would sell on a rising market and stock up on a falling market. Now we have a turnover six times a year.

Mr. Miller: The unfortunate thing is that on a fluctuating price level the average man has got to take speculative action.

Governor Strong: I have just gotten a report from New York. We have credited the clearing house this morning $93,000,000, on top of $100,000,000 yesterday. Call money is at 2 ½ per cent, with $20,000,000 offered. The stock market is having a rise and Government securities are weak. The Treasury has made repayment to us.

Thereupon the Governor adjourned the meeting at 12:40 p.m.

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