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Final minutes

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MINUTES OF MEETING OF THE OPEN MARKET POLICY CONFERENCE
HELD AT THE OFFICES OF THE FEDERAL RESERVE BOARD
WASHINGTON, D. C., JANUARY 21, 1931.

The meeting convened at 10:00 o'clock, there being present the following:

Governors Young, Fancher, Seay, Black, McDougal, Martin,
Geery, Talley, Calkins and Harrison, Chairman
Deputy Governors Hutt, Worthington and Burgess, secretary.

The preliminary memorandum submitted by the chairman and the report of the secretary covering System operations in government securities were distributed and read by those present. It was moved and carried that these reports be received and placed on file.

"Governor Harrison then reviewed for the conference his discussions with European bankers and others and the impressions he gathered on his recent European trip. In the course of extended discussion of these matters Governor Harrison pointed out that the world owes the United States on balance about $600,000,000 each year, and that payment has to be made in gold, in imports from foreign countries to us, or by borrowing from us. These countries were unable to send us much more gold, their exports to us were now limited and new financing curtailed. Their only alternative was to diminish their purchases of goods from us, which was now being done to our detriment.

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He indicated that the people he met abroad appeared to believe that recovery from the present business depression depends largely on America, partly for psychological reasons and partly because of the importance of exports to us and borrowing from us.

Generally speaking he felt that the economic situation of European countries had grown distinctly worse since his visit last spring, and has probably grown somewhat worse in the weeks since his recent return from Europe.

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After general discussion with regard to the foreign situation, Governor Harrison referred to the reduction of the discount rate of the Federal Reserve Bank of New York, effective December 24, 1930. He indicated that the banking situation was of primary importance in the decision. He had been urged from many quarters to make a reassuring statement which might aid in quieting the banking situation. Such a statement was practically impossible because to be strong enough to do any good it would run the risk of being contradicted by any small bank failure which might thereafter occur. The rate reduction, apart from other reasons, served as a method of stating to the public that money was freely available. The rate reduction was justified technically by the money situation. It would probably help the foreign situation as well as the domestic situation. Incidentally, it might make it easier for France to reduce her rate. The discount rate decision had been made very rapidly, and there had not been an opportunity to discuss the matter with most of the other Reserve banks. In fact, the proposal had only arisen after the meeting on December 20 of the executive committee of the Open Market Policy Conference.

Governor Harrison referred to the holdings of sterling bills purchased during the period of greatest weakness of sterling last autumn. He said it had been the intention to sell these bills some time after the turn of the year, when it was hoped that sterling would be strong enough to make that an orderly operation. Recent weakness of sterling, however, has made this program seem undesirable up to this time, and instead of the sale of sterling the directors of the New York bank had voted at their last meeting to sell a part of the securities which had been added to the portfolio of the New York bank during the recent banking emergency.

Governor McDougal commented on the recent discount rate change by the Federal Reserve Bank of Chicago and indicated with regard to the last three changes in their discount rate that in the case of the first two of these changes it had been hoped that the reduction in the rate would have some encouraging effect upon business, but that the latest change had been made without any such belief, but was designed to correct to some extent the large differential of 1 1/2% between the Chicago rate and that of the New York bank.

Governor McDougal expressed the hope that there would be no further reduction in the bill rate; that money was too cheap with Federal funds quoted at 1/4 of one per cent; and that it would be better for the market to get the bills if it wanted them.

Governor Calkins suggested that the position should be one in which we kept our bill rate low, but tried to correct any over-sloppy condition in the money market by the sale of government securities. Several of those present concurred in this view.

There ensued a discussion as to the statement of facts in the preliminary memorandum submitted by the chairman, and Governor Harrison further reviewed the changes in the money market since the last meeting of the Open Market Policy Conference, pointing out that the seasonal expansion in the requirements for Federal reserve credit up to the time of financial disturbances had been less than normal, and bill purchases appeared to be sufficient to take care of seasonal needs without additional purchases of government securities. This appeared to be true, until the banking emergency when the New York bank had found it necessary to take over securities from two member banks and at the end of the year when purchases were necessary in order to avoid too great tightening of credit due to an unusual amount of "window dressing." Purchases made for the open market account had since been liquidated as had also $20,000,000 of the emergency purchases made by the New York bank. Since the turn of the year the return flow of funds appeared to have greatly aided the bond market. There had been a considerable excess of reserves of the New York City banks, though this had fluctuated a good deal. It was the general plan of the New York bank to liquidate the balance of the temporary purchases of $45,000,000 of securities, as the surplus of reserves offered opportunity without interfering with the bond and money market.

It was moved by Governor McDougal that it was the sense of the conference that the present was an opportune time to let government securities go from the open market portfolio as and when it could be done without undue disturbance, with the understanding that sales should not be made rapidly and should be made in orderly fashion. Governor McDougal explained this motion by saying that some time ago System open market operations had followed a general principle which he believed to be sound, and should be reverted to, that whenever the market is ready to take bills and government securities the Reserve System should sell them, and conversely, the System should acquire them when the market cannot take them readily. On this principle he would like to hold bill rates where they were to push bills out of the System.

Governor Harrison commented that if we sell governments we should have the bill rate at a point nearer to the market so that we might be ready to take in bills without such a big penalty to the seller. He would not favor any sales of governments unless the bill window were opened to provide in this way any money the market required.

There ensued a general discussion as to how a general policy might be stated in which Governors Harrison, Black, Young, and Seay participated, all of them agreeing that a statement of policy as well as proposed action was important.

Governor Young stated that a sale of $50,000,000 or $60,000,000 of governments might perhaps injure the bond market; that a comercial banker who saw a reduction in government holdings of the Reserve System would be inclined to sell bonds. In any event it was important to decide the general policy whether the conference favored firmer or easier money, or the status quo.

Governor Black presented a substitute resolution to that of Governor McDougal, the provisions of which were then discussed.

The morning meeting adjourned at 1:10.

The meeting reconvened at 2:37, and after further discussion the following resolution was adopted by unanimous vote:

> "The Conference has considered the preliminary memorandum submitted by the Chairman and has reviewed business and credit conditions as they now appear. It is the sense of the Conference that in view of these conditions it should be the policy of the System to continue an easy money policy in the best interest of trade and commerce. It is the belief of the Conference, however, that the seasonal return flow of currency and credit and other factors have tended during recent weeks to make for an undue excess of funds in the principal money centers. It is therefore the opinion of the Conference that in these circumstances it would be desirable to dispose of some of the System holdings of government securities as and when opportunity affords itself to do this without disturbance or any (undue *) tightening of the money position. It is understood that there shall be a new meeting of the Conference as soon as or whenever conditions in the opinion of the Conference or the Federal Reserve Board justify a reconsideration of this policy."
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> * this word later omitted

While this resolution was being typed, Governor Harrison reported briefly his appearance before the Senate sub-committee investigating monetary problems.

At 4:30 Governor Meyer and Messrs. Hamlin, James, Miller, and Goldenweiser, McClelland, and Smead joined the meeting.

Governor Harrison reviewed the discussions of the Conference, read the preliminary memorandum of the chairman, and the resolution stating the findings of the conference. He also reported the action of the directors of the Federal Reserve Bank of New York in voting to sell $35,000,000 of government securities out of the emergency purchase made during December, of which amount $20,000,000 had already been sold.

Mr. Miller inquired whether the banks of other districts than New York had surplus reserves. Governors Young and McDougal replied that the banks in the Boston and Chicago districts did not have surpluses. Mr. Miller inquired how surplus reserves were to be interpreted, and Governor Harrison replied that they appeared to indicate first, little demand for funds by borrowers, and second, reluctance to employ funds. He stated that the New York banks were in a very liquid position, their per cent of liquid assets being as high as perhaps ever before. Governor McDougal stated that the three largest banks in Chicago showed a very liquid statement, probably never exceeded in liquidity.

Governor Harrison said that the recent test in New York of the ability of certain banks to stand losses of 30% to 50% of their deposits raised the question of the desirability of the Federal Reserve System having power to discount notes secured by listed bonds under proper safeguards. He believed such a provision might make it much easier to deal with cases of banks facing runs.

Mr. Miller suggested that the banking situation might be suffering just now from excessive caution and excessive desire for liquidity. Governor Harrison replied that that was one reason why our easy money policy had not proved more effective. Governor Meyer suggested that money was not really easy until last summer, and that the expected good results from easy money had been interrupted by bank failures and other difficulties.

Mr. Miller referred to a memorandum which he had received relating to the possible use of Clearing House certificates and discussing the liquidity of the city banks, which was then read by the assistant secretary of the Federal Reserve Board.

Governor Meyer stated that the banking situation was at present the primary thing to consider, and that whatever policy was adopted should be adopted with that in view. He suggested that bill maturities would respond to changes in the money market, and would act as a buffer in taking up surplus funds. Any proposal for the liquidation of governments should consider the present extraordinary reluctance of banks to show bills payable. The present banking situation was so delicate that it could be easily disturbed.

Governor Harrison pointed out that the resolutions of the conference represented a compromise since some of those present were in favor of considerable sales of securities, while others were only in favor of such moderate sales as might be necessary to take up some of the slack. Governor Meyer suggested that any move which the Federal Reserve System made in its automatic assets immediately put the acts of the System on the skyline where they were subject to observation and criticism.

Governor Harrison indicated that he would not be content with even the proposed moderate program of sales of governments unless the buying rates for bills were nearer to the market rate, as bills coming back to the System would act as a safety valve in case too much funds were withdrawn from the market.

Mr. Miller stated that the banking situation was now more important than the credit situation, and asked what the governors were planning to do in different districts if further banking trouble started. The Federal reserve bank is the normal place of leadership, and plans should be developed to keep any bank with good resources from suffering.

Governor Harrison outlined a method which had been devised in New York to deal with any banks which might hereafter be in trouble.

At this point Governor Harrison left the meeting.

Governor Meyer stated that a reduction of bills and discounts of the System did not involve the launching of any major policy, whereas the sale of governments is commonly interpreted as a major move in Federal reserve policy. The Reserve System has been accused in a number of quarters of pursuing a deflationary policy in the past year, and a sale of government securities at this time is likely to draw fire. In this situation it would appear most desirable to avoid a move which appears to represent a major change in policy when there is no necessity for doing it.

Governor Young said that those present would certainly not favor any program which they believed would affect bank confidence, or that was a new and major change in policy. Government bonds had first been bought under an emergency, and their purchase had proved helpful, but there was a limit to what the System could do in buying bonds. Some sales would put the System into a position to go back into the market and buy again if it is necessary.

Governor McDougal pointed out that no one present was desirous of dumping securities in the market, but they favored a program that would be worked out gradually. Governor Calkins stated that he believed the word "undue" should be omitted in the phrase "any undue tightening of the money position." There seemed to be general sentiment in favor of this suggestion.

Governor Meyer stated that in this position the Board has an apparent responsibility to the country; that the world was now in the worst economic condition that he had ever seen. There had been the worst breakdown in credit conditions which he had witnessed. The present situation in Germany and Australia in which a nation's credit was at question being cases in point. Unemployment, unrest, and discontent were severe. Under these circumstances everything which the Federal Reserve System does which is or may be interpreted as a move in major policy is on the skyline.

Governor Calkins stated that the proposal was not considered as a major change in policy, that his idea was that a beginning of sales might be made by letting February 16 maturities of Treasury bills run off. It could not be considered a major change in policy because it provides specifically for the "continuance of an easy money policy."

The meeting adjourned at 6:15.

W. Randolph Burgess,
Secretary.