Internal Memorandum

Owen D. Young Papers

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EC - #26

Box 265

Melvin
~~Morgan~~ Traylor of Chicago, President of the First National Bank of Chicago, on July 26, 1928 writes Mr. Young "that the President in the last few days has been furnished with some illuminating statistics calculated to convince him that in view of the large refunding operations which the Secretary of the Treasury contemplates this fall the policy of the Federal Reserve Board with regard to open market operations is a great detriment to the government.

'It is claimed that the facts presented His Excellency are certain to be convincing and that by the middle of August or not later than the first of September the banks will begin accumulating outside investments and will continue that policy until there is a marked relief of the credit situation, the prediction being a reduction in the Federal Reserve discount rate to at least 4 1/2% and possibly 4% by the middle of September." Mr. Traylor is alarmed.

Mr. Young replies on August 3, 1928 saying, "That the Federal Reserve System has more credit in the market than the business of the country needs is to my ~~m~~mind clear. The use of the excess amount has been to overstimulate buying of stocks and bonds. Our policy of cheap money a year ago I think was sound then to strengthen the foreign exchanges and stimulate the buying of our surplus for export and to make money cheap for the movement of our crops. After that was over, we should have stiffened our rates and discouraged further extension of credit by actions, say, in November instead of February. We delayed too long, and we did not drive with quite stiff enough hand after we started on the program of restraint. As a consequence we have two things to do; one is to discourage the further use of credit, and the other is to get considerable liquidation of the volume outstanding. Through the action of the last few months the Reserve Banks, I think, have put a stop to further extensions but they have not succeeded in getting much liquidation. They hoped for rather quick liquidation in the stock market, but they hoped in vain because stocks are well margined, and as you said in Chicago, the bond market rather than the stock market is the worst offender in the abnormal use of credit. That is now becoming clear to everybody. Getting liquidation through the bond market will, of course, be a slow process, which means that the original program of getting momentarily high rates and quick liquidation and then cheap money for crop movements and business in the autumn will not materialize."

This is a highly important letter in its bearing on the situation which preceded both Strong's death and the 1929 panic. It might well be referred to as a commentary on the period and the situation.

MA:IB