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January 28, 1941.

Dear Dan:

Enclosed is a brief memorandum commenting on the first draft of the Secretary's proposed statement before the Ways and Means Committee on Wednesday in regard to H. R. 2653.

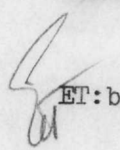
Following the Secretary's telephone conversation yesterday morning and immediately upon receipt of the copies of his proposed statement, I discussed it with the staff. In the very limited time since then, I have not had an opportunity to take it up with the Board or to undertake to do more than prepare the enclosed memorandum.

Sincerely yours,

M. S. Eccles,
Chairman.

Honorable Daniel W. Bell,
Under Secretary of the Treasury,
Washington, D. C.

enclosure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FOR FILES
E. H. McKnew

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January 28, 1941.

MEMORANDUM ON THE SECRETARY'S PROPOSED STATEMENT TO THE WAYS AND MEANS COMMITTEE, JANUARY 29, 1941, ON H. R. 2653.

This is merely a summary memorandum on H. R. 2653 and the first draft of the proposed statement of the Secretary to the Ways and Means Committee. The statement is essentially explanatory and factual, rather than an argument for the various proposals contained in the bill. In the limited time it has not been possible to take up the bill and the proposed statement with the Board or to make a thorough analysis.

With regard to the legislation, there are three major sources of funds that, I think, the Treasury should be in a position to tap: (1) the great bulk of smaller savings that would be reached by savings bonds and certificates on about a 3 per cent basis; (2) the large and increasing idle cash balances of large corporations and wealthy individuals that are not likely to go into long terms but would be reached by 90-day to 9-month bills and one to two-year notes on a basis of 1/4 to 1 per cent, depending on the maturity; (3) institutional investors such as insurance companies and the various types of fiduciary institutions interested in long issues, possibly some form of registered bond, giving them at least 2-1/2 per cent.

The proposed bill seems to be adequate to permit the Treasury to tap the first source. The second one can be reached only when the excess reserves problem is dealt with and the short-term rate structure increased accordingly. As to the third category, the question is whether the proposed bill gives the Treasury enough authority. In this connection I attach a brief memorandum prepared by George Vest, Assistant General Counsel of the Board. With his first suggestion I am in accord. As to his second one, I am passing it along for your information.

With regard to the Secretary's proposed statement, I would suggest one or two changes. At the top of page 3, I would refer to "expansion" rather than "inflation" of bank deposits. On page 4, second paragraph, I would omit the sentence reading, "The money market at that time afforded the Treasury an excellent opportunity to refund the large maturities and raise the additional cash needed largely through sale of long-term bonds." This seems to me extraneous and not necessary to the point you are making, and it is contrary to the position I took in December. One possible implication is that the Government should take advantage of an artificial money market situation which it is mainly responsible for creating. You would want to avoid that implication, I am sure, because the Government with its powers to control the rate and its responsibility to its customers is not like a private corporation in marketing securities.

With regard to long-term bonds, as I pointed out in a memorandum in connection with December financing, many uncertainties will overhang the market until we know what Congress does in connection with the excess reserves problem, banking and tax legislation, and the proposal to make future issues of government securities fully taxable. As I said in that memorandum, "Until these questions are settled, the market cannot be expected to measure long-term interest rates with fairness. With the removal of the influence of large surplus banking funds on the market, long-term rates, which are now at record low levels, might increase somewhat to a

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"point that would more nearly reflect the level necessary for attracting the savings of the country. If a long-term bond should be issued at the present time it would be vulnerable to an increase in rates. If this condition is anticipated it may be more in the public interest to protect investors from impairment in market value by deferring the issuance of long-term bonds until after such an adjustment has occurred."

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