September 27, 1946

To: Chairman Eccles

From: David M. Kennedy and
Richard A. Musgrave

As an alternative to eliminating the buying and repurchase rate on Treasury bills and permitting the rate to rise to say 3/4 per cent, you might want to renew your proposal for a single 9-month, 3/4 per cent security to replace bills and certificates. Such a security would have many advantages:

1. It would not increase the level of interest rates since it would be priced at approximately the market.

2. It would simplify short-term financing through substitution of a single for two issues, which in effect are both demand obligations.

3. It would simplify open market operations making it unnecessary to support two short-term rates. The System would then maintain only the 3/4 per cent and 2 1/2 per cent rates and permit the rest of the market to take care of itself.

4. It would provide flexibility to banks in making adjustments for deposit fluctuations.

5. It would reduce bank earnings by a small amount.

The proposal could include provision for exchange of the System's holdings of 3-month Treasury bills into a special low-rate security. Even without this provision the cost to the Treasury would be only about 2 million dollars more per year than under the present 3/8 per cent bills and 7/8 per cent certificates.

DMK RAM