

December 14, 1943

Mr. J. W. Peyton, President,
Federal Reserve Bank of Minneapolis,
Minneapolis, Minnesota.

Dear John:

I was very much interested in your letter of December 8, outlining a method of reducing Treasury redemptions of savings bonds in the immediate post-war period by making savings bonds marketable issues. After thinking about this suggestion, however, it seems to me that it is open to a number of serious objections. These objections are as follows:

*sent to
Gen. Film
12/17/43*

1. It might accelerate a shift in holdings of Government securities from individuals to commercial banks. The highest rate of return on savings bonds is in the last few years of their life, amounting in the case of Series E bonds to $\frac{1}{4}$ per cent in the last five years. The prospect of obtaining high rates on short-term and intermediate-term securities would encourage commercial banks to bid actively for savings bonds. Such a development would be particularly unfortunate in a period when inflationary pressures may be strong. At the end of the war, there is likely to be considerable demand from the public for the removal of war-time restrictions. In fact, such demand is already evident. The combination of a premature removal of restrictions, large amounts of bank deposits and liquid investments, and at least temporarily an inadequate supply of consumer goods will create sufficient problems without encouraging individuals to dispose of their savings bonds.
2. If commercial banks paid to holders the redemption price or even somewhat above the redemption price, they would be subject to criticism on two counts: first, that they were making an unreasonably high return on Government securities

and, second, that they were taking advantage of small, uninformed investors.

3. A change that made savings bonds marketable would no doubt increase their value to the original purchasers, but the fact that their terms were changed might be looked upon with suspicion by small investors, many of whom remember the large discounts to which Liberty Bonds declined in the market after the last war.
4. There are already quotations on about 80 issues of marketable securities. If savings bonds should be made marketable, it would be necessary to add to these quotations at least one for each six-month period that Series E bonds have been outstanding, amounting to 18 additional quotations at the present time, and at least one for each six-month period that Series F and G bonds have been outstanding, amounting to 12 additional quotations. It seems to me that there are now so many individual Government issues for which quotations must be maintained that it would be undesirable to add further to the number.
5. To the extent that savings bonds are sold, there would be an advantage from the point of view of the Treasury in having these sales in the form of redemptions at the Treasury. Regardless of whether savings bonds are sold in the market or redeemed at the Treasury, holdings of Government securities will be transferred from individuals to commercial banks. If savings bonds are redeemed, the Treasury can replace them with securities at a lower rate of interest. Consequently, the Treasury will be able to reduce the cost of financing the debt. The high interest cost on savings bonds is willingly borne at the present time because of the influence that sales

of savings bonds have in controlling inflation. If the country is deriving no benefit from these securities, as would be the case if they were sold by individuals to commercial banks, there would no longer be any reason for the Treasury continuing to pay a subsidy rate of interest on these securities.

Perhaps you have already considered these points and have come to the conclusion that the advantages that you mentioned would offset these disadvantages. It seems to me, however, that the reverse is true and that the proposal would create more difficulties than it would solve. That is the way it sounds on my piano.

Sincerely yours,

M. S. Eccles,
Chairman.

LMP:msk