

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date August 22, 1946.

To Chairman Eccles

Subject: Commercial bank purchases of

From Mr. Knapp

International Bank bonds.

With reference to our telephone conversation yesterday concerning possible action by the Comptroller of the Currency in the matter of International Bank securities, I would strongly recommend that you defer any action on this matter until you return. I am sure that this question will not arise for the Comptroller of the Currency in active form until late this year or early next year; in all probability not until the International Bank has filed a registration statement for its first issue of debentures and is about to make its first offering. At that time I agree that it will be desirable to have the N.A.C. consider the matter.

In general, member banks are entitled under existing laws and regulations to invest 10 per cent of their capital and surplus in securities issued or guaranteed by the International Bank, provided that such securities are considered by bank supervisors to be of investment quality (this limitation applies in the case of all national banks and in the case of almost all State banks). Theoretically, member banks in this country might purchase up to 650 million dollars of such securities, but in practice the aggregate amount would no doubt be much smaller, and during 1947 purchases of such securities by commercial banks are unlikely to exceed say 150-200 million dollars.

There is no doubt that by any objective test International Bank securities must be regarded as of investment quality and not as "distinctly or predominantly speculative". Furthermore, it is probable that sooner or later the Comptroller of the Currency will have to pass upon the quality of these securities for commercial bank investment. There is considerable question as to whether the private rating agencies will undertake to rate them, and probably a test case would soon arise in the course of bank examinations. The question therefore boils down to this: Should the Comptroller of the Currency make a ruling as to the investment quality of the securities before he has to, i.e. at or about the time of the initial offering?

Specifically, what should the Comptroller of the Currency do if at the time of the Bank's initial offering some commercial bank writes him to ascertain whether the securities being offered are eligible for bank investment? Such an inquiry may be confidently expected. Should the Comptroller of the Currency respond favorably, realizing that his reply even though not publicly released would receive wide circulation in the banking community and encourage investment in these securities by commercial banks?

The judgment as to how to handle such an inquiry at the time of the offering involves weighing two considerations: (1) our desire to encourage a favorable reception of International Bank securities offered in this market, and (2) our desire to minimize the expansion of bank credit or the shift of

bank credit from short-term Governments to long-term securities. It may be that in view of the latter objective we should not go out of our way in any respect to encourage commercial bank subscriptions to these securities. At the same time, we must be careful to avoid any action (or omission) which might lead the public to believe that International Bank securities were not of investment quality.