FEDERAL RESERVE BANK

OF DALLAS

Dallas, Texas, January 18, 1946

AMENDMENT TO REGULATION U

To All Banking Institutions in the
Eleventh Federal Reserve District:

There is transmitted herewith a supplement to Regulation U, issued by the Board of Governors of the Federal Reserve System, effective January 21, 1946, which raises margin requirements to 100 per cent.

This requirement relates only to future purchases and sales of registered securities. It does not apply to the use of credit for any purpose except to finance transactions in securities. The rule incorporated in Regulation U, effective July 5, 1945, will, in view of the new 100 per cent margin stipulation, now require that whenever securities held as collateral to regulated loans are sold the proceeds must be used to reduce or retire the borrower's indebtedness. Except to this extent, the regulation does not require reduction or liquidation of existing loans.

It will be recalled that the regulation is not applicable to loans for purposes other than purchasing, carrying, or trading in securities registered on a national securities exchange.

In connection with the action of the Board of Governors in amending Regulation U (and T), there is quoted below the text of a statement which was given to the press for release on January 17, 1946:

Statement for the Press by Chairman Eccles

"My personal view of the Board's decision to increase margin requirements to 100 per cent may be summed up as follows:

By this action, the Board has used its authority to prevent the further flow of borrowed money into stock market operations. There is no further recourse left to the Board, so far as restraining speculative activities in listed stocks is concerned, except possibly to order that all existing margin accounts be put on a cash basis and to make some of the administrative provisions applying to banks more rigid. To whatever extent the Board's action will tend to dampen speculative activity, it is desirable, as a preventive step, at this time of strong inflationary pressures and until such time as inflationary dangers are passed.

As I have frequently sought to emphasize in the past, the primary source of the inflation danger which overhangs the domestic economy on all fronts is the vast accumulation of currency and bank deposits at the disposal of the public as a result of the fact that far too much of the cost of the war was financed through the creation of commercial bank credit and not enough was financed out of taxes and the savings of the public. Credit for stock market as well as other purposes has been curbed all along, but it is a minor and not a major factor in the inflation picture. While credit curbs are justified for such restraint as they may impose on speculative activities in a time of inflationary danger, they cannot reach the real source of danger, which is the huge amount of money already created through bank credit. Price controls, rationing, allocations, etc., are vitally necessary for holding the line until the danger is past, but they are not designed to prevent the excessive money supply from flowing into speculation in capital assets, such as homes, farms, business properties and securities.

The most effective way that I know of to curb speculation in capital assets would be to increase substantially the rate of the capital gains tax, or the holding period, or a combination of both. For a long time I have advocated enactment of legislation to this end as a temporary protective measure applicable to all future purchases. This would not deter the selling of assets held at the time the measure was introduced in Congress, but it would greatly deter buying for the speculative rise after that date. It would not affect the purchase of capital assets of any kind which have been or are being bought for personal use or long-term investment rather than for the speculative rise.

In addition, it is important to point out that so long as the public debt continues to be monetized through the purchase of government securities by the banking system, the supply of money will continue to increase, thus tending further to reduce the interest rate on savings and investment funds. The resultant pressure of an increasing money supply and of lower interest rates is bound to have a further inflationary effect upon all capital assets and to increase the difficulty of holding down the cost of living.

It is, therefore, imperative that the process of further monetizing of the public debt through the banking system be ended so that the rate of return on investments would be stabilized and would reflect the supply of savings and investment funds in relation to the demand instead of reflecting an increasing amount of bank credit. This process needs to be stopped not only by bringing about a balanced budget, but also through measures to check further unnecessary expansion of commercial bank holdings of government securities.

Only by a vigorous, comprehensive attack along the entire economic front can the battle be successfully waged against inflationary pressures. Credit curbs are at best supplementary and not basic measures for reaching the underlying causes of these pressures."

Banks which are members of the Federal Reserve System are requested to insert the attached amendment in the ring binders containing Regulations of the Board of Governors and Bulletins of this bank.

Yours very truly,

R. R. GILBERT

President

Amendent No. 6 to Regulation U
Issued by the Board of Governors
of the Federal Reserve System

The Supplement to Regulation U is hereby amended to read as follows:

SUPPLEMENT TO REGULATION U

ISSUED BY THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

Effective January 21, 1946

For the purpose of section 1 of Regulation U, no stock, whether or not registered on a national securities exchange, shall have any loan value.

Loans to Specialists.—Notwithstanding the foregoing, a stock, if registered on a national securities exchange, shall have a maximum loan value of 50 per cent of its current market value, as determined by any reasonable method, in the case of a loan to a member of a national securities exchange who is registered and acts as a specialist in securities on the exchange for the purpose of financing such member's transactions as a specialist in securities.