

FEDERAL RESERVE BANK
OF DALLAS

Dallas, Texas, June 28, 1946

To the Managing Officer of the Bank Addressed:

The program of the Government for the financing of the war emphasized that banks should not make loans to facilitate speculative purchases of Government securities. On October 8, 1945, prior to the Victory Loan, the Secretary of the Treasury addressed a letter to all banks in the United States in which the banks were requested to decline to make loans for speculative purchases of Government securities and to decline to accept subscriptions from customers which appeared to be entered for speculative purposes. I also wrote you in regard to this matter on October 15, 1945.

It was recognized, however, that there would be instances in which purchasers of securities for investment and not for speculation would want to anticipate income by borrowing temporarily from banks. It was understood that these loans would be repaid out of income and would have maturities of not to exceed six months. Loan arrangements of this character were recognized in the joint statement issued by the National and State Bank Supervisory Authorities in 1942 which said that "Such loans will not be subject to criticism but should be on a short term or amortization basis fully repayable within periods not exceeding six months."

During the Victory Loan, a large amount of long-term bonds was purchased with the aid of bank loans. It has been reported that many such loans have not been repaid out of current income and that bank credit has been used for speculative carrying of Government securities. Reports have been received also of the activities of money brokers and others seeking to arrange bank loans on Government securities for clients without provision for amortization and with margins and rates of interest which emphasize high returns on small amounts of the borrower's own funds required for relatively large transactions. The same general considerations which had led to efforts to discourage speculative subscriptions for Government securities during the war loan drives clearly apply to this sort of loan.

Borrowing from banks creates an addition to the country's money supply to the same extent as direct purchases of securities by banks. The existing unprecedented supply of deposits and currency, in the face of an inadequate supply of goods and services, is a dangerous inflationary potential and, therefore, every effort should be made to reverse the wartime trend of increased borrowing for the purpose of purchasing and carrying Government securities and to reduce as much as possible the use of bank credit for that purpose. This important objective will not be accomplished if loans which are paid at one bank are merely transferred to other banks.

Sincerely yours,



R. R. Gilbert

President