9/11/1927

The Chicago Rate Controversy

Please Note: The original papers will be kept for archival purposes in a separte folder in the departments Discount Rate Changes files.

Please Note:

For the Date 9/11/1927

The Chicago Rate Controversy
Shall be filmed in
its entirety. Dates may
appear out of date.-
There are special guides the
tell you the Start of the Chicago
material and the END.-
rest of work will continue
in date order after that.

9/11/1927

The Chicago Rate Controversy

Includes Files on;

1. Strong Memorandum Relative to Chicago Rate Controversy
2. Correspondence with Members of Committee and other FR Banks Re: Transactions in Open Market Account
3. Open Market Investment Committee Meeting 5/9/1927 and 7/27/1927
4. Correspondence with Phila. + Chicago FR Banks Relative to lowering of Rediscount Rate
5. Cables and Correspondence with Foreign Bks. of Issue Re: Discount Rate
6. Samples of Corres. with other FR Banks Relative to Foreign Credits
7. Extracts from Articles of Chicago Clearing House Ass. and N.Y. Clearing House - Relative to Interest on Deposits.
8. Governors Conference - 1/20-23/15
9. Opinions Relative to Right of FR Board to Initiate Changes in Discount Rate
10. Copies of Corres. Relative to Purchase and Sale of Gold + Sterling Exchange (1927)

(A) MEMORANDUM RELATIVE TO THE CHICAGO RATE CONTROVERSY

9/11/1927

THE CHICAGO RATE CONTROVERSY

This memorandum is prepared solely for the use of Mr. J. S. Alexander - New York member of the Federal Advisory Council - to aid in the discussion of the above matter at the Council meeting to be held in Washington on September 16, 1927. This statement and the documents attached are confidential, not to be published, entered in any record of the meeting, nor distributed to the members. Mr. Alexander will use his own discretion in making references to or reading from the papers.

The discussion will be confusing unless care is exercised to separate the three very distinct questions involved, to wit -

1st. The merits of the policy of lower discount rates.

2nd. The general method employed to adopt a system policy of lower rates.

3rd. The particular method employed in the case of Chicago.

But before discussing these questions it is necessary to refer to some erroneous current reports as to the motives which may have actuated the Federal Reserve Bank of New York. Those which have currency are mainly, -

(a) To aid the Treasury's program for the 15th September financing.

(b) To aid the Bank of England.

(c) To support stock speculation.

As to (a). When Mr. Mellon first took office in March, 1921, he held the view that our rates were too high and might be reduced. He was probably right - but never urged that view. It was discussed more than once early in 1921. From that time to the present neither he nor his assistants have ever urged, requested, or suggested any change of rate, or any policy as to open market operations. We have always considered it our duty as Fiscal

Agents to keep the Treasury fully informed as to our policy and have done so. It has always been initiated free of Treasury suggestion or influence, and we have never proposed or volunteered policies beneficial to Treasury financing which were not based upon sound consideration of Federal Reserve policy. At the time of the July 27 meeting of the Open Market Committee, when a change was to be proposed, the matter was reported to Mr. Mills, then Acting Secretary in Mr. Mellon's absence, but he refrained from advice even, and said that he would observe the policy of not interfering with any Treasury consideration. He attended the meeting in Mr. Mellon's absence, and when asked by me if he cared to discuss the subject of rates and open market policy, he declined on the ground that the Treasury should not attempt to influence the decision. So far as the Federal Reserve Bank of New York is aware, the Treasury under Mr. Mellon has scrupulously pursued this policy of non-interference.

As to (b). The relations between the Federal Reserve Bank of New York and the Bank of England are little understood and frequently misrepresented. It has been our purpose and policy, so far as might be possible consistent with our own position, to aid in the resumption of stable monetary conditions, stable exchanges, and the reestablishment of the gold standard in Europe. We believe that this policy is sound and not only aids in the restoration of world trade and prosperity, but particularly in the preservation of our own markets abroad, and full employment and prosperity at home. There has never been any obligation, express or implied, to aid the Bank of England or any foreign bank of issue when such aid is incompatible with our domestic welfare. Any suggestion to the contrary must be based upon ignorance

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But since 1924 and 1925 it has been in the power of the Federal Reserve Bank of New York at any time, by rate advances and by a dear money policy - to break down this very structure of stability we have been striving to erect. Withdrawal of foreign balances by American banks, closing our markets to foreign loans, causing large exports of gold to New York, and forcing dangerously high bank rates in Europe, could easily destroy all that has been accomplished. The penalty for us would be a recurrence of disordered exchange, and a loss of our export trade - no less in food stuffs and cotton than in manufactured goods. Europe and the Bank of England are dependent upon us - not we upon them - and unless we recognize that fact and avoid a hostile or destructive policy we shall suffer consequences about as serious as those we could inflict.

As to (c). It is hardly necessary to refute a charge that we aim to promote speculation or protect the speculator. But I have no hesitation in expressing some views on this puzzling complication in our situation. There is no doubt that the liquidation of 1920 and 1921 and the depreciated value of the dollar still remaining after liquidation was concluded, left both fixed interest and equity investments below their real values, considering the still reduced purchasing power of the dollar, that is, gold, and considering also the generally lower level of interest rates prevailing. During the past few years a gradual, and latterly a rapid, readjustment of these values has been under way. It has been much accelerated by the enormous savings of the country, producing an unsatisfied demand for investments, urgently reinforced by the release of from $500,000,000 to a billion dollars of funds each recent year for reinvestment, due to the repayment of the Government war loans. The same development occurred to a less extent in the real estate and building boom which reached its climax last year. These readjustments were bound to take place and to be largely financed by borrowings. Fixed interest investments have now greatly advanced and become more nearly stabilized; but speculation as was to be expected, has been centered upon common stocks, although recently both the rate of advance of prices and of growth of loans have been somewhat reduced. The real question is whether we should ignore all other objectives of policy and direct our efforts solely to checking stock speculation. If so, we have the choice either of high rates or of some form of direct aggressive action. It is our opinion that either course would involve policies which could not be supported on the ground of our primary responsibility, which is not the stock market, and if successful in reducing the speculation would have had other consequences, as above and later suggested - too grave to face. The Federal Reserve System was no more organized to regulate the prices of stocks than it was to regulate the price of cotton or real estate or pig iron or wagees or rents. And during most of these last two years, there has been no commodity speculation and the price level has declined.

One great peril to the Federal Reserve System is the assumptio n, by the System, or by the public, that it can manage or regulate or in some way control these isolated and special movements, such as speculation in stocks or real estate, or advances or declines in prices of individual commodities. The demand that we should curb stock speculation is one manifestation of this tendency. Once we submit to this demand, we must submit to all others and our responsibilities will crush us. The pending bill attempting to charge us with the duty of price control is no less an evidence of this tendency.

As to 1st. Merits of the Rate Change.

The justification of our policy is to be found in four or five simple facts. One is that we are dependent upon Europe for a market for our marginal production of export goods, mainly cotton, automobile, wheat, meats, oils, and copper.

Another that we shall lose that market if monetary disorder, exchange troubles, high interest rates and price declines abroad force liquidatio n there.

A third is that we cannot sell our surplus abroad during these years of recovery without extending credit.

A fourth is that Europe already has heavy obligations to meet in the United States for war loan payments and the service of private loans, no less in fact than a billion dollars a year.

And finally, that a restrictive credit policy will force gold shipments to this country in default of other means of payment.

Let us briefly examine these facts. The first is illustrated by cotton, the most important export we have. Last year we grew our largest crop on record, 18,000,000 bales, of which we exported ~~$~~11,000,000 bales, within two million and a half of this year's total estimated crop,-and one-half of our exports went to England. Had the world not been able to borrow about one and one-quarter billion dollars here that year, we could not have sold all that cotton. This applies equally to the meat animals, which consume the corn crop, and automobiles and other export goods, upon which the Chicago district largely depends for its prosperity.

No discussion of the adverse influence of monetary disorder upon international trade is necessary before a meeting of bankers. On that subject the world has expressed a unanimous opinion. A depreciation in the values of Europe's currencies after the good progress made toward stability would mean a brief period of artificially stimulated exports by Europe, curtailment of our exports and then collapse - and world wide alarm.

The need for credit aid to Europe during reconstruction is shown by simple facts. In the last few years we have loaned over $5,000,000,000 net abroad, and during that period have had no net exports of gold. The only way the borrowed dollars could be used was to spend them in buying American goods. So except for the balances left with our banks, all this borrowed money has been used to pay for our goods. Had we not loaned it the goods would have been unsold, unless they had been paid for in gold. We have maintained a lending market at reasonable rates and kept our trade going and our people employed.

The liquidation of war obligations to our Government and meeting service of loans privately held calls for gross payments of about a billion dollars a year, - less what applies to securities repurchased by foreign investors, - some fraction of the whole. Pending the gradual restoration of trade, elevation of living standards, increased capacity to consume and increased exports by Europe, these payments are now possible only by borrowing, mainly in the United States. That is feasible only if rate relationships here and abroad are such as to make borrowings not only possible, but not so costly as to impoverish the debtors. In time the adjustments of production and trade and of services to be paid for - or possibly even readjustments of debts, will enable these payments to be made without unsupportable strain on central bank reserves. But in these years of recovery our credit is not only needed but essential, and undue curtailment means a stoppage of payment and disaster.

Finally, if credit is restricted in the United States and other means of payment for new goods and old debts fall, we shall be paid in gold to the extent gold can be spared. So far we have succeeded in avoiding a perilous gold inflation, and we can probably continue to do so if we are fairly liberal as well as careful in lending. Once we stop we will drain Europe of large amounts of her gold, inflation here will be unavoidable and we shall then face another period of worldwide monetary disorder - Europe drained of gold, we glutted with it.

There are decided advantages to be gained other than those relating to our trade, by deferring the test as to whether war debts can be met without break down of monetary systems. The Dawes plan has so far proved to be a success, but it must be remembered that the entire payment so far made by Germany has been borrowed abroad, mostly here, and even 25 per cent or more in excess of these payments. The fourth annuity year just commenced will likely impose no strain which cannot be met. In the fifth year commencing September, 1928, the full payment of $625,000,000 is to be made, and then the test will arise. If Germany cannot pay her creditors, they may not be able to pay us. The plan provides means for certain capital payments which can be employed to ameliorate the burden. Political considerations indicate that an adjustment of that character will be unlikely until the German, French, and American elections, all occurring in 1928, are out of the way. So a policy which maintains the present equilibrium in the meantime is justified on that account as well.

It will naturally be asked - what relation has all this to the Chicago (which also applies to the Philadelphia and San Francisco) discount rate. The answer is in New York money rates and their relation mainly to London rates.

With the Chicago rate at 4 per cent., and New York at 3 1/2, we can expect and believe we now observe three tendencies.

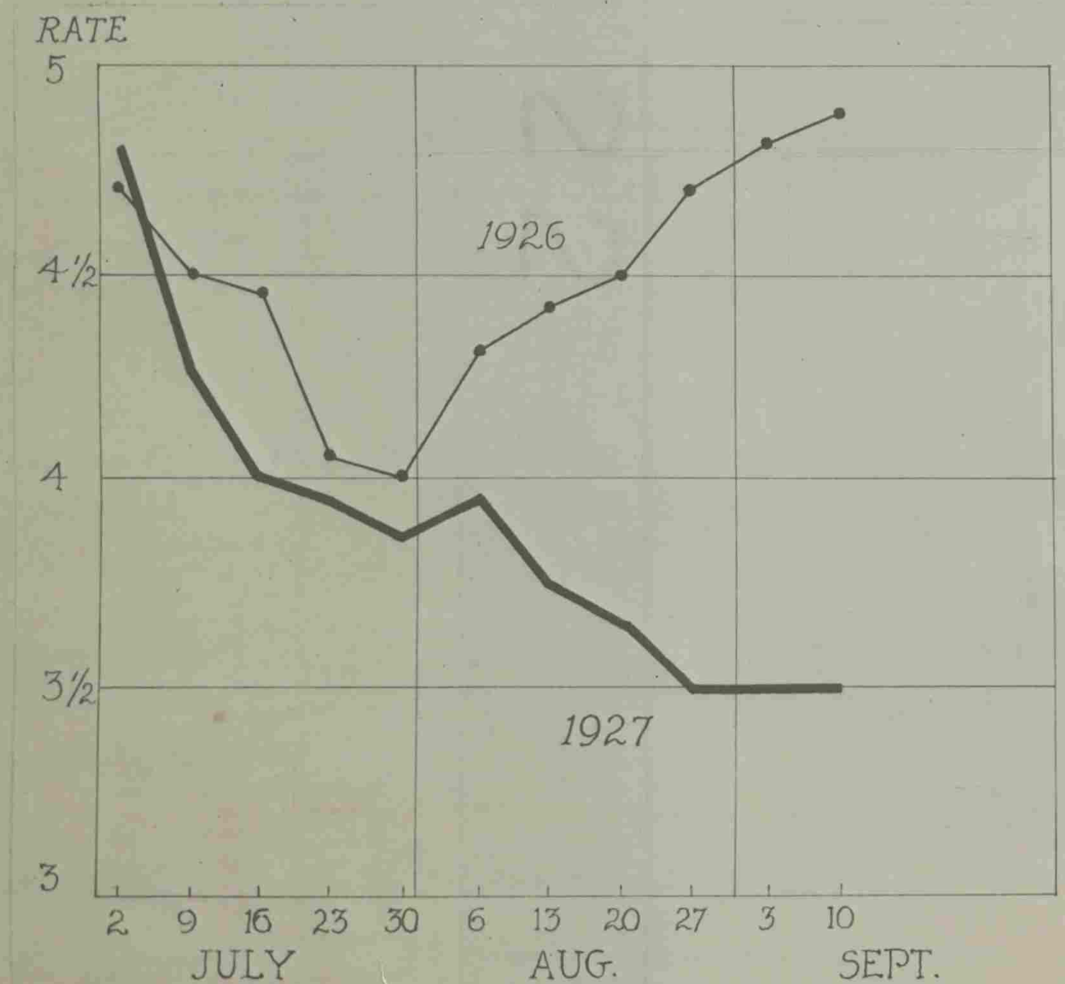
1st. Bank balances carried in New York tend to move to higher rate districts.

2nd. Interior banks (and other borrowers also) tend to increase borrowings in New York, where rates have now somewhat cheapened.

3rd. Money employed in Stock Exchange loans at 3 1/2 per cent tends to be drawn home to the interior - especially by member banks, which at this season need to borrow from the Reserve Bank.

This all tends to accentuate the usual seasonal demand on New York banks, impairs their reserves, forces larger borrowing from us, and may cause higher rates for money than can be continued without forcing advances in discount rates abroad. The operation of these tendencies is illustrated in the following chart and table. The chart on reserves indicates that the Second District lost 188 million dollars to other districts between July 1 and September 7.

Gold Reserves, Federal Reserve Bank of New York.



Average Call Money Rate (Renewal).

Loans to Brokers and Dealers - Secured by Stocks and Bonds

(000 Omitted)

1927	For Own Account	For Account out-of town Banks	For Account of Others	Total
July 6	$1,105,949	$1,155,799	$864,579	$3,126,327
13	991,498	1,204,315	863,466	3,059,279
20	981,769	1,202,644	874,561	3,058,974
27	1,047,608	1,187,441	906,144	3,141,193
Aug. 3	1,109,556	1,189,518	872,771	3,171,845
10	1,063,670	1,216,369	910,290	3,190,329
17	1,022,037	1,248,136	918,796	3,188,969
24	1,000,961	1,246,848	920,265	3,168,074
31	1,045,669	1,222,914	915,475	3,184,058
Sept. 7	1,046,074	1,238,325	921,900	3,206,299
1926				
July 7	1,019,298	951,852	631,638	2,602,788
14	932,813	1,016,148	652,296	2,601,257
21	954,368	1,018,361	648,223	2,620,952
28	933,881	1,014,859	653,302	2,602,042
Aug. 4	994,572	1,024,766	669,379	2,688,717
11	936,741	1,089,093	692,498	2,718,332
18	918,775	1,104,676	718,937	2,742,388
25	941,544	1,072,654	717,012	2,731,210
Sept. 1	991,437	1,098,091	668,746	2,758,274
8	963,901	1,134,421	664,707	2,763,029

Discussions with the officers of at least five or six European central banks, as well as our own observations, convince us that the importance of the relative rate level between New York and London and some of the continental money centers, is greater than is generally understood. For some months after we advanced our rate to 4 per cent, thus reducing the differential to roughly 1/2 per cent, sterling and continental exchange rates were maintained above their gold export points. This was largely due to our loans to foreign borrowers. Early this year, however, an unseasonable drain upon European reserves started, and so far this year we have imported net about $145,000,000 of gold. As the season of active exports of American food products and cotton approached it appeared that very much larger imports of gold were likely. We learned that the heads of two important continental banks of issue were consulting the Bank of England regarding a policy of rate advances by all three on that account. Our rate reduction at least deferred and possibly prevented general advances abroad.

Something of the influence of our rate reduction may be seen in the strength of sterling this August and September compared with a year ago. The average monthly rates have been as follows:

	1926	1927
July	4.8589	4.8518
August	4.8540	4.8563
September (1-10)	4.8514	4.8574

If the drain on New York from other parts of the country causes such advances as to much reduce the present differential of 1 per cent between New York and London money rates, we will either be forced to buy large amounts of securities in New York so as to reduce rates, or take in more of Europe's gold - until finally they are forced to advance discount rates. Our policy would then fail.

It must not be understood that the Chicago rate is itself fatal to our policy. We could adjust our plans to meet a 4 per cent rate there. But it will be easier now that they have reduced.

Evidence was and is still accumulating that there is some slowing down of business in certain lines, notably iron and steel and automobiles, beyond the usual seasonal recession. This is usually a condition in which rate reductions can do no harm and may be helpful. A reduction of our seasonal exports would greatly accelerate a business recession.

Finally, we have a great advantage in our 3 1/2 per cent rate in case an advance later becomes necessary. Marking up rates from a 4 per cent starting point would be much more dangerous than if we start from the 3 1/2 per cent level.

As to 2nd. The Method Employed to Adopt a System Policy of Lower Rates.

This will involve narrating the events of the last few months.

On May 9 a meeting of the Open Market Investment Committee was held in Washington, at which the whole situation was reviewed, and it was decided to purchase, as need appeared, not over $100,000,000 of securities, the program to terminate August 1. We have rarely held a meeting where discussion and exchange of views was more complete and it fully covered the European problem. The situation was also set out in writing, and the statement has been sent to all Reserve Banks and the Federal Reserve Board.

Between June 28 and July 20 we had meetings in New York with Governor Norman of the Bank of England, Dr. Schacht of the Reichsbank, and Dr. Rist and Monsieur Ricard of the Bank of France, and reviewed the entire situation with them. Governor Crissinger and all the members of the Open Market Investment Committee spent a day in New York with these gentlemen, and discussed the situation fully. Governor McDougal heard all of the discussion, took part in it, and then reviewed it separately with the officers of the Federal Reserve Bank of New York, even to the point of himself suggesting that Governor Strong or Mr. Harrison go to Chicago to discuss the whole matter with his directors.

The gentlemen from abroad met our directors, individually and at meetings, and our directors heard all aspects of the problem discussed. They spent a day, July 7, in Washington and discussed the situation with members of the Federal Reserve Board. All those responsible were called into conference, given opportunity to ask questions, and all questions asked were freely answered by our visitors.

Finally, as our authorization to make open market purchases was expiring on August 1, a meeting of the committee was held in Washington, all being present, on July 27. In addition the Governors of the Federal Reserve Banks of Kansas City, St. Louis, and Minneapolis attended, and the Chairman from St. Louis. Again a written memorandum was submitted, and a discussion lasting all day covered the entire subject. No more complete or enlightening exchange of views could have been possible. The position of the Federal Reserve Bank of New York was briefly as follows: We were convinced that the time was at hand when we should reduce our rate to 3 1/2 per cent. We felt that to make the reduction effective we might need to purchase additional securities, say $50,000,000. We invited those present to discuss our rate proposal without reserve. We did <u>not</u> suggest that other banks should reduce their rates. Governor Crissinger, supported by other members of the Board, <u>did</u> suggest that the change should first be made in the Middle West. We stated that it was not material to us who reduced first - nor even essential that all should reduce. We felt it would be most helpful and was possibly necessary, for some other reductions to be made - especially Boston, Philadelphia, Cleveland, and Chicago. We would wait, or reduce first, as might be agreed.

The meeting was unanimous as to a reduction in New York. Governor McDougal said his directors would not then be in favor of a rate reduction in Chicago and certainly would not take the lead, though they might follow if conditions changed. Some of the other governors expressed the view that local conditions alone did not then justify lower rates, but that as a matter of general system policy they favored a reduction. Still others favored reduction in their banks on both grounds.

When Governor Crissinger and the members of the Open Market Committee were in New York, Governor Crissinger suggested that he and I should visit Cleveland and Chicago for the purpose of meeting the directors of those two banks and explaining the situation personally. He raised the question again either by telephone or when I was next in Washington. I thought it over, consulted my associates here, and decided that it would be unwise for me to appear before the directors of any other Reserve Bank for the purpose of discussing a rate change by that bank, and accordingly wrote Governor Crissinger, copy of my letter on that subject being among those accompanying this memorandum.

Over three months has been devoted to these meetings and no change of policy by the System has ever been canvassed more thoroughly than was this one. For convenience of reference a chronology of the discussions is inserted here.

Chronology of Events Leading to Rate Reductions

May 9, a meeting of the Open Market Investment Committee was held in Washington at which a memorandum was submitted discussing this whole situation, and this resulted in the authorization of purchases of $100,000,000 Government securities in the open market, of which, however, only about $30,000,000 were purchased.

June 28, Dr. Rist and M. Ricard of the Bank of France arrived in New York, having come for the purpose of discussing the whole central bank problem and the relations between the European and American money markets.

July 1, Governor Norman of the Bank of England and Dr. Schacht of the Reichsbank arrived in New York for the same purpose. Following the arrival of these gentlemen continuous discussion took place as we immediately left New York and spent five or six days at a private house on Long Island.

July 6, Messrs. Norman, Schacht, Rist, Ricard and Strong went to Washington and spent most of July 7 in discussion with the members of the Federal Reserve Board, lunching with them at the Hotel Willard.

July 8, the members of the Open Market Committee, Messrs. Harding, Norris, Fancher, McDougal and Strong, together with Governor Crissinger, spent the day in New York, most of it devoted to a discussion of these same subjects with Messrs. Norman, Schacht and Rist. Thereafter the visitors from abroad left on different dates, the last, Governor Norman, sailing on July 20.

July 27, a meeting of the Open Market Investment Committee was held in Washington for the purpose of reviewing the whole rate situation, especially in the light of the meetings previously held, and also because the authority to purchase securities up to $100,000,000 was expiring on August 1. In addition to all the members of the Open Market Investment Committee and the members of the Federal

Reserve Board then in Washington (Dr. Miller and Mr. Cunningham were away) there were present Governors Young of Minneapolis, Biggs of St. Louis, Mr. Martin, chairmanof the Federal Reserve Bank of St. Louis, and Dr. Burgess Harrison of the Federal Reserve Bank of New York. Governor Bailey was in Washington the day previous when Governor Strong was also there, in order to discuss the situation with the Federal Reserve Board, and left at once for Kansas City as his meeting occurred the following day and he had to return in order to lay the matter before his directors. At this meeting of the Open Market Investment Committee a memorandum was submitted similar to the one submitted at the meeting of May 9.

Following this discussion, on July 29, the Federal Reserve Bank of Kansas City reduced its rate to 3 1/2 per cent. A few days later the Federal Reserve Bank of Boston reduced its rate, requesting the Federal Reserve Board to make the announcement simultaneously with the announcement of the rate reduction in New York when that occurred.

On August 5, the Federal Reserve Bank of New York reduced its rate to 3 1/2 per cent, and that reduction, together with the Boston rate was announced on the same day.

The other changes were made in the following order:

Cleveland,	August	6
Dallas,	"	12
Atlanta,	"	13
Richmond,	"	16

On September 7, two meeting days having elapsed in Chicago, the Federal Reserve Board reduced the Chicago rate to 3 1/2 per cent and announced it.

On September 8, Philadelphia reduced.

On September 10, San Francisco reduced.

September 9 and 10, Governor Strong was in Washington on other matters having to do with the Treasury Department, his visit there having been arranged by Mr. Parker Gilbert prior to the action by the Federal Reserve Board in reducing the Chicago rate, and his visit there was not a result of the Board's action or in any way related to it.

September 12 Minneapolis reduced.

<u>As to 3rd. The particular method employed in the case of Chicago.</u>

There may be little gained by discussing the meaning of the law as to rate changes. At best it is indefinite. I have never been willing to believe that Congress intended the Federal Reserve Board to initiate rate changes. But on the other hand no formula appears for cases where changes having been disapproved, a new rate must be fixed, or where a new rate can be fixed, if an existing rate is not changed by the directors. It does seem, however, that Congress would hardly have required the vote of five out of seven members of the Board to fix rates for rediscounts between Reserve Banks, an infrequent and relatively unimportant occurrence, and then give unlimited authority to initiate changes of discount rate, our most important act, by vote of a majority only.

This has been a matter of controversy from the start. Early in 1915 the Governor of the Minneapolis Reserve Bank, by order of his directors, reported to a meeting of the Governors that the Federal Reserve Board had attempted to force a reduction in their rate. The Governors passed a resolution unanimously protesting, and suggested testing the question in the courts. This never became necessary, but I was told that an opinion, possibly informal, was asked of the then Attorney General who did not sustain the Board. This I have never had confirmed nor has such an opinion even been published.

In 1919, for practically the entire year, and with increasing insistence in the autumn, the Federal Reserve Bank of New York advised and urged rate advances. The Board never approved our doing so, clearly their right, but then also the opinion of the Attorney General was asked and Acting Attorney General King wrote an opinion upholding the Board's present contention that they could initiate a change.

In 1915, the Federal Reserve Bank of New York obtained an opinion from John G. Johnson of Philadelphia, who, as I recall, held that the Board could not initiate a change but could determine a rate different from one established by a bank and sent to the Board for review.

In 1920, White and Case rendered an opinion that the Board, under its general supervisory powers, could initiate a rate change. These opinions are attached.

The nearest case to initiating a change by the Board of which I have heard, was also in Chicago where the directors, on learning of the Board's intention, acted promptly enough so that an issue was avoided.

Ext. personal / for Mr Alexander.

In the present instance our relation to the Chicago rate change has already been explained save on one point. After seven or eight banks had reduced their rates, Governor Crissinger telephoned me that Chicago had declined to do so, that the Board had disapproved the continuance at 4 per cent, and at a meeting to be held on Tuesday, September 6, proposed to make their rate 3 1/2 per cent. I stated to him that I hoped the Board would not do so as I doubted the wisdom of that course as well as the Board's power. Tuesday morning he 'phoned me that the Board would act that morning. I suggested that Mr. Mellon was in New York and asked whether they could not wait one day until he reached Washington, when the full Board would be available. He asked me to see Mr. Mellon and get his views. This required time to go uptown, which I did, explained the situation fully to Mr. Mellon and asked his views. He said he hoped the Board would await his return Wednesday morning, and he would see the Governor at once on his arrival. When I 'phoned this to Governor Crissinger soon after 12 o'clock (after 11 Washington time) on that Tuesday he said that the Board had already acted, the wire was being or would be sent, and he thought it would add to the difficulty were he to report my talk with the Secretary. I did ask him to think it over again if not too late.

The Federal Reserve Act is lamentably lacking in separating and defining the respective powers of the Board and the Banks. It would be far better, however, to find means of adjusting different views just now than to attempt a series of amendments such as may well result from this controversy, or than to attempt arbitrary action which invites controversy which is detrimental to the System.

My own judgment is that the Board is too detached from the scenes of operation and from operation problems, money markets and all the complexities of the business to wisely initiate changes of discount and open market policy or attempt their execution. A nice balance can best be found after more experience. If the Act must be changed - then a limited power to initiate, - say upon a specified number of majority votes, and only in a case where an individual bank is recalcitrant, - might be granted to the Board.

There is one point upon which there must be no misunderstanding. It has been too frequently published in recent Chicago press articles to be ignored.

There is no desire and never has been any conscious attempt by the Federal Reserve Bank of New York to dominate the Board or the System. We have in the past and shall in the future, urge views upon our associates, as we expect them to do with us. We are ready to submit our individual views to the authority of the Board where it is clear the Board has authority, and I know of no case where we have failed to conform to System policies, even when our individual views were contrary to those of the other Reserve Banks. The practical question is how policies are to be adopted and then executed. Our views are clear enough. Expressing the problem, in one extreme there is the choice of complete centralization of power to initiate policy and direct its execution in the Federal Reserve

Board, - or at the other extreme, complete decentralization, with power in each bank to conduct its business in each district in a watertight compartment, with no System policy! Either would be fatal to the System.

The plan has gradually evolved, so as to escape either danger, of arriving at policies by agreement at meetings of the Governors and Chairman, or of Committees of those and other officers. The most important committee is the one on Open Market investments. This committee was first appointed by the Conference of Governors, but in 1923 the Board arbitarily, without previous notice, dismissed the committee, and reappointed the same men as a committee with largely the same functions, but with an attempt to subject it completely to the Board's control. That was a mistake which caused much unnecessary controversy and friction, though there now exists a much better working understanding. My position as chairman of that committee has seemed to everyone necessary, as the New York bank, in the principal money, security and foreign exchange market, must execute most of the orders.

The alternative here again is for the New York bank to ignore the other Reserve Banks, develop and execute its own policy, or subject itself to some supervision and enjoy with other Reserve Banks some sort of cooperation in a System plan, through committee supervision.

This latter we have done as scrupulously as possible. Repeated inquiry of members of the committee and of the banks not represented on the committee convinces us that they are satisfied and approve not only the plan but the way the New York bank executes the committee's wishes and directions.

This committee now has supervision of -

(a) All open market purchases and sales of Government securities, save strictly intra-district transactions, with member banks. (But even transactions with members, the Federal Reserve Bank of New York voluntarily makes a part of the committee account).

(b) All purchases and sales of bills.

(c) The distribution of these two investments between the Reserve Banks.

(d) Operation of all foreign accounts (banks of issue) which are ratably divided.

(e) All investments for foreign account.

(f) All special foreign transactions, such as the credits to the Bank of England, Bank of Belgium, and Bank of Poland.

(g) All gold transactions abroad.

(h) And as a matter of courtesy, and because changes in the New York rate of discount probably have more effect upon other districts than their changes have in New York, we have never, since the committee came into existence, made a change of rate without first consulting the committee either at a meeting, or by letter, or by telephone.

(B)

Correspondence w/
members of Committee
and other FR Banks RE:
transaction in Open Market
A/C

C O P Y   O F   T E L E G R A M

Dallas 1034A JUNE 24

CASE NY

IN VIEW OF INCREASED EXPENSES INCIDENT TO OPERATIONS OF OUR NEW SAN ANTONIO BRANCH IF OPEN MARKET COMMITTEE HAS NO OBJECTION WE WOULD LIKE TO INCREASE OUR HOLDINGS OF FOURTH $4\frac{1}{4}$s IN AMOUNT OF $1,000,000 WE OBSERVE PRICE OF FOURTHS HAS BEEN STEADY FOR SEVERAL DAYS PAST AT 103.23 IF YOU DO NOT KNOW ANY REASON WHY WE SHOULD NOT DO THIS WILL APPRECIATE YOUR BUYING $1,000,000 FOR US SOMEWHERE AROUND PRICE I HAVE MENTIONED PLEASE ADVISE

TALLEY

COPY OF TELEGRAM

TALLEY
DALLAS

JUNE 24, 1927

WE SHALL OF COURSE PURCHASE $1,000,000 FOURTH LIBERTY LOAN 4¼% BONDS IF YOU WISH US TO, BUT IT HAS OCCURRED TO US THAT, IN VIEW OF YOUR RECENT LETTER TO HARRISON REFERRING TO SIZE YOUR GOLD SETTLEMENT FUND, YOU MIGHT PREFER TO POSTPONE PURCHASE ESPECIALLY IN VIEW OF FACT ALL YOUR SHARE OF GOLD IN LONDON WILL SHORTLY BE EARNING APPROXIMATELY 4% OR SLIGHTLY MORE. STOP FURTHERMORE, OPEN MARKET INVESTMENT COMMITTEE WILL PROBABLY MAKE REAPPORTIONMENT OF PURCHASES EARLY NEXT MONTH

CASE

C O P Y   O F   T E L E G R A M

DALLAS   JUNE 24   356PM

CASE

IN VIEW OF YOUR COMMENT IT IS JUST AS WELL TO DROP MATTER FOR PRESENT AT LEAST. ALTHOUGH OUR GOLD SETTLEMENT BALANCE IS AMPLE FOR NEEDS AND IT IS UNLIKELY THAT TRADE BALANCES WILL RUN AS HEAVILY OR AS ACUTELY AGAINST US THIS SUMMER AS WAS THE CASE LAST YEAR, OUR MATURING BILLS BETWEEN NOW AND 30TH ARE $2,000,000 THE RETIREMENT OF WHICH WILL IMPAIR OUR COLLATERAL ACCOUNT WITH AGENT TO THAT EXTENT AND UNLESS COMMITTEE IS GENEROUS IN ALLOTMENTS TO REPLACE OR NEXT REAPPORTIONMENT DOES NOT FULLY COVER OUR REQUIREMENT WE COULD MAKE PURCHASE OF ADDITIONAL GOVERNMENTS MENTIONED WITHOUT ANY SERIOUS INCONVENIENCE TO OUR COLLATERAL ACCOUNT AGSINST NOTE ISSUES, NOW WOULD IT PROBABLY REDUCE OUR GOLD SETTLEMENT FUND BALANCE BELOW REQUIREMENTS. MATTER OF PURCHASE CAN BE DEFERRED UNTIL AFTER COMMITTEES REAPPORTIONMENT EARLY NEXT MONTH

TALLEY   916AM   25th

O P Y

Similar letter sent to: Governor Norris, Philadelphia)
Governor Fancher, Cleveland) Members of Open Market
Governor McDougal, Chicago) Investment Committee

June 27, 1927.

Dear Governor Harding:

Enclosed you will find a statement showing the gross and net earnings of all banks for the first five months of 1927 and also estimated similar figures for the last seven months, from which it appears that all of the banks, except Richmond and Minneapolis, will have earnings during 1927 sufficient to cover all charges. The deficiency in the case of Minneapolis is very small, while that in the case of Richmond is comparatively large.

It will be noted that the present estimated net earnings of the System for the year, after all charges are $2,777,000. Column "4" of the statement shows the net earnings of each bank for the year as at present estimated, while column "6" shows the distribution of these earnings in the proportion that each bank's expenses, dividends and chargeoffs bear to the System total. A comparison of these figures would indicate that with one or two exceptions, notably Richmond, no more than minor adjustments are necessary in the distribution of future purchases of bills.

This statement does not include the income which will presently be received from the investment of the foreign credit resulting from the sale of French gold. The income to the System from this source during the balance of this year is likely to be something over $1,000,000. While these earnings will be distributed among all the banks, it will not affect the comparative showing as disclosed by the statement enclosed.

There is also attached a memorandum showing in comparative form three ratios for each of the banks as follows:

1. Ratio of each bank's expenses, dividends and chargeoffs to the System total.

2. Present holding ratio of Government securities including System investment account.

3. Ratio of earnings required other than from Government securities during balance of year 1927 to cover expenses, dividends and chargeoffs.

Assuming that the estimates which have been made by the banks as to their earnings and expenses for the balance of this year are reasonably correct, the use of the ratios shown in the third column of this memorandum in distributing future purchases of bills would effect such adjustments as are necessary to enable all banks to fully cover their charges for 1927.

We suggest, therefore, that these ratios be used in making future distributions of bills purchases, and if this action meets with your approval and that of the other members of the Open Market Investment Committee, the change will be made as soon as we are so advised and all the Reserve banks approve. If the change meets with the approval of the members of the Committee, we will, of course, write each of the governors, advising fully as to the changes which are being made, at the same time advising of the possibility of similar minor changes from month to month, if the revised figures hereafter submitted by the banks indicate that further changes are necessary.

An expression of your views will be appreciated as promptly as possible.

Very truly yours,

BENJ. STRONG,
Chairman, Open Market
Investment Committee.

Mr. W. P. G. Harding,
Governor, Federal Reserve Bank of Boston,
Boston, Massachusetts.

Enclosures.

MEMORANDUM SHOWING IN COMPARATIVE FORM
FOR THE TWELVE FEDERAL RESERVE BANKS
RATIOS AS INDICATED

	Ratio of Each Bank's Expenses, Dividends and Charge-offs to the System Total	Present Holding Ratio of Government Securities Including System Investment Account	Ratio of Earnings Required Other Than from Government Securities During Balance of Year 1927 to Cover Expenses, Dividends and Charge-offs
Boston	7	3.7	8
New York	24	17.	28
Philadelphia	8	7.4	8
Cleveland	10	13.1	8
Richmond	5	2.8	8
Atlanta	4.5	2.7	5
Chicago	15	14.6	15
St. Louis	5	8.1	4
Minneapolis	3	5.	3
Kansas City	5.5	8.3	4
Dallas	4	6.6	3
San Francisco	9	10.7	6
	100	100	100

STATEMENT OF ESTIMATED GROSS AND NET EARNINGS FOR YEAR 1927
(5 months actual - 7 months estimated)
(000 Omitted)

	Gross Earnings	Expenses and Dividends	Estimated Year-end Charge-offs	Net Earnings	Ratios of Expenses, Dividends and Charge-offs to System Total	Distribution of Net Earnings on Ratios of Expenses Dividends and Charge-offs
Boston						
Actual for 5 months	$1,178	$ 1,086		$ 92		
Estimated for 7 months	2,022	1,482	162	378		
" Total	$3,200	$ 2,568	$162	$ 470	7%	194
New York						
Actual for 5 months	4,036	3,641		395		
Estimated for 7 months	6,045	5,191	475	379		
" Total	$10,081	$ 8,832	$475	$ 774	24%	666
Philadelphia						
Actual for 5 months	1,288	1,249		39		
Estimated for 7 months	2,076	1,686	62	328		
" Total	$3,364	$ 2,935	$ 62	$ 367	8%	222
Cleveland						
Actual for 5 months	1,716	1,425		291		
Estimated for 7 months	2,420	2,054	285	81		
" Total	$4,136	$ 3,479	$285	$ 372	10%	278
Richmond						
Actual for 5 months	663	750		87		
Estimated for 7 months	959	1,132	147	320		
" Total	$1,622	$ 1,882	$147	$ 407	5%	139
Atlanta						
Actual for 5 months	844	696		148		
Estimated for 7 months	1,241	926	135	180		
" Total	$2,085	$ 1,622	$135	$ 328	4.5%	125
Chicago						
Actual for 5 months	2,571	2,182		389		
Estimated for 7 months	3,599	2,963	x 697	61		
" Total	$6,170	$ 5,145	$697	$ 328	15%	417
St. Louis						
Actual for 5 months	854	694		160		
Estimated for 7 months	1,370	1,039	317	14		
" Total	$2,224	$ 1,733	$317	$ 174	5%	139
Minneapolis						
Actual for 5 months	543	477		66		
Estimated for 7 months	735	723	102	90		
" Total	$1,278	$ 1,200	$102	$ 24	3%	83
Kansas City						
Actual for 5 months	916	805		111		
Estimated for 7 months	1,326	1,176	166	16		
" Total	$2,242	$ 1,981	$166	$ 95	5.5%	153
Dallas						
Actual for 5 months	636	618		18		
Estimated for 7 months	944	917	41	14		
" Total	$1,580	$ 1,535	$ 41	$ 4	4%	111
San Francisco						
Actual for 5 months	1,679	1,326		353		
Estimated for 7 months	1,951	1,757	251	57		

Boston						
Actual for 5 months	$1,178	$ 1,086		$ 92		
Estimated for 7 months	2,022	1,482	162	378		
" Total	$3,200	$ 2,568	$162	$ 470	7%	194
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Dallas						
Actual for 5 months	636	618		18		
Estimated for 7 months	944	917	41	14		
" Total	$1,580	$ 1,535	$ 41	$ 4	4%	111
San Francisco						
Actual for 5 months	1,679	1,326		353		
Estimated for 7 months	1,951	1,757	251	57		
" Total	$3,630	$ 3,083	$251	$ 296	9%	250
GRAND TOTALS	$41,612	$35,995	$2,840	$ 3,208	100%	$2,777
				431		
				$ 2,777 Net		

* Includes possible loss $400,000

C O P Y

Similar letter sent to: Governor Seay, Richmond
" Wellborn, Atlanta
" Young, Minneapolis
" Biggs, St. Louis
" Bailey, Kansas City
" Talley, Dallas
" Calkins, San Francisco

June 30, 1927

Dear Governor Seay:

Enclosed you will find a statement showing the gross and net earnings of all banks for the first five months of 1927 and also estimated similar figures for the last seven months, from which it appears that all of the banks, except Richmond and Minneapolis, will have earnings during 1927 sufficient to cover all charges. The deficiency in the case of Minneapolis is very small, while that in the case of Richmond is comparatively large.

It will be noted that the present estimated net earnings of the System for the year, after all charges, are $2,777,000. Column "4" of the statement shows the net earnings of each bank for the year as at present estimated, while column "6" shows the distribution of these earnings in the proportion that each bank's expenses, dividends and charge-offs bear to the System total. A comparison of these figures would indicate that with one or two exceptions, notably Richmond, no more than minor adjustments are necessary in the distribution of future purchases of bills.

This statement does not include the income which will presently be received from the investment of the foreign credit resulting from the sale of French gold. The income to the System from this source during the balance of this year is likely to be something over $1,000,000. While these earnings will be distributed among all the banks, it will not affect the comparative showing as disclosed by the statement enclosed.

There is also attached a memorandum showing in comparative form three ratios for each of the banks as follows:

1. Ratio of each bank's expenses, dividends and charge-offs to the System total

2. Present holding ratio of Government securities including System Investment Account

3. Ratio of earnings required other than from Government securities during balance of year 1927 to cover expenses, dividends and charge-offs.

Assuming that the estimates which have been made by the banks as to their earnings and expenses for the balance of this year are reasonably correct, the use of the ratios shown in the third column of this memorandum in distributing future purchases of bills would effect such adjustments as are necessary to enable all banks to fully cover their charges for 1927.

All the members of the Open Market Committee have approved the use of these ratios in making future distributions of bill purchases and it is proposed to begin their use as soon as approval is received from the Governors of the other banks. I shall therefore appreciate receiving your reply by wire in order that the change may be put into operation at an early date. It is possible that there may be similar changes from month to month, on the same basis, if the revised figures hereafter submitted by the banks indicate that further changes are necessary.

Very truly yours,

BENJ. STRONG
Chairman, Open Market
Investment Committee

Mr. George J. Seay,
Governor, Federal Reserve Bank of Richmond,
Richmond, Va.

C
O
P
Y

FEDERAL RESERVE BANK

OF ST. LOUIS

July 6, 1927.

Dear Governor Strong:

We have your letter of June 30th, and inclosures, from which it is noted that in making future distributions of bills purchased, it is proposed to give this bank 4% of the total purchases. This ratio is satisfactory to us.

Very truly yours,

(Signed) D. C. Biggs

Governor

Bejn. Strong, Esq., Chairman,
Open Market Investment Committee,
Federal Reserve Bank of New York,
New York.

C
O
P
Y

FEDERAL RESERVE BANK

OF RICHMOND

July 6, 1927.

Dear Mr. Case:

I am today in receipt of your telegram answering mine of yesterday relating to the distribution of System investments. and note your statement that the ratio of distribution will be changed monthly to meet the requirements, and that if the pro rata of this bank does not meet the requirements, the Committee will make proper adjustment, which is, of course, entirely satisfactory.

I had out controller examine carefully the distribution plan and he reported that, while the ratio of distribution to the expenses of our bank in proportion to the total expenses of the System was liberal, the ratio in proportion to our need of revenue in comparison with other Federal Reserve Banks was too small. It has been the practice, I believe, in recent times, to adjust the ratio according to the apparent needs of revenue after such needs had become sufficiently clear.

With kind regards, I am

Very truly yours,

(Signed) Geo. J. Seay

Governor.

Mr. J. H. Case, Deputy Governor,
Federal Reserve Bank of New York,
New York City.

C
O
P
Y

T E L E G R A M

7G D SAN FRANCISCO JULY 7 320P

STRONG NEW YORK

Changed ratio for future distribution purchases of bills your letter June Thirtieth acceptable to us

CALKINS 911A 8th

C
O
P
Y

TELEGRAM

162G D DALLAS 1148A JULY 7

STRONG NEW YORK

Referring your letter June 30 proposed ratio for future distribution of bill purchases satisfactory to this bank. On account of double holiday and my absence from city letter was not answered sooner.

237P TALLEY

C
O
P
Y

T E L E G R A M

142G D ST. LOUIS 1128A JULY 7

MATTESON

Wrote Governor Strong under date of sixth that distribution of bills purchased to give this bank four percent was satisfactory to us.

BIGGS 203P

C
O
P
Y

T E L E G R A M

229G BO MINNEAPOLIS JULY 7 235PM

MATTESON

Just returned from the west to find Governor Strong's letter of June 30. Rates suggested agree.

YOUNG 448P

C
O
P
Y

July 7, 1927.

Dear Governor Seay:

I have your letter of yesterday acknowledging my telegram regarding the distribution of system investments, and note that the ratio which it is proposed to use for your bank is satisfactory with, of course, the understanding that it is subject to change as and when conditions may make necessary.

It has been the aim of the committee to distribute the earning assets purchased by it in an equitable way and in such a way as will be satisfactory to all of the banks, and I do not anticipate there will be any difficulty in continuing this program.

Very truly yours,

(Signed) J. H. Case

Deputy Governor

Mr. Geo. J. Seay, Governor
Federal Reserve Bank of Richmond
Richmond, Va.

COPY

FEDERAL RESERVE BANK

OF ATLANTA

July 5, 1927.

Mr. Benj. Strong, Chairman,
Open Market Investment Committee,
c/o Federal Reserve Bank of New York,
New York, N. Y.

Dear Governor Strong:

Referring to my telegram of even date, I am pleased to advise that this bank concurs in the use of the ratios enclosed with your letter of the 30th ultimo, in making future distributions of bill purchases.

Very truly yours,

(Signed) M. B. Wellborn
Governor

C

OPIC.
meeting 5/9/1927
+
7/27/1927

(1)

MINUTES OF MEETINGS OF OPEN MARKET INVESTMENT COMMITTEE HELD IN WASHINGTON, D. C., DURING WEEK OF GOVERNORS CONFERENCE, COMMENCING MAY 9, 1927

The Open Market Investment Committee held a meeting in Washington, D. C., at the office of the Federal Reserve Board, Monday, May 9, 1927, at 9 o'clock.

Present:

Governor Strong, Chairman
Governors Harding, Norris, McDougal
and Fancher
Mr. Harrison, Acting Secretary

The secretary read the preliminary draft of the memorandum of matters to be considered by the Open Market Investment Committee prior to the preparation and submission of a report and recommendations. After discussing the preliminary memorandum it was the opinion of the committee that copies of it with suggested amendments should be submitted by the chairman of the committee to the Federal Reserve Board for its consideration in order to familiarize the Board with the factors which would be in the minds of the committee later in preparing its report.

The Open Market Investment Committee adjourned at 10 o'clock.

* * * * * * *

The Open Market Investment Committee reconvened on Monday, May 9, 1927, at 12:30 o'clock.

Present:

Governor Strong, Chairman
Governors Harding, Norris, McDougal
and Fancher
Mr. Harrison, Acting Secretary

The committee considered a redraft of the preliminary memorandum containing the amendments agreed to at the earlier meeting. With these amendments, the chairman was requested to transmit seven copies of the memorandum to Governor Crissinger for the members of the Board, with the advice of the committee that the committee would be glad to meet with the Board to discuss the memorandum at any time suitable to its convenience. These copies of the report were transmitted to Governor Crissinger at 1:15 o'clock, when the Open Market Investment Committee adjourned.

* * * * * * *

The Open Market Investment Committee met with the Federal Reserve Board on Monday, May 9, 1927, at 4:10 o'clock.

Present:

Governor Crissinger
Messrs. Platt, Miller, James, Hamlin, Cunningham of the Federal Reserve Board
Governors Strong, Harding, Norris, McDougal and Fancher
Dr. Goldenweiser
Mr. Harrison, Acting Secretary

There was a long discussion by various members of the committee and the Federal Reserve Board of the preliminary memorandum previously distributed among the members of the committee and the Federal Reserve Board. Governor Strong explained that this preliminary memorandum did not embody any recommendations but merely raised points for discussion with the Reserve Board which would enable the committee later to file a report with definite recommendations. In connection with the consideration of the memorandum and problems before the committee, Dr. Goldenweiser gave his statement of the present business situation with particular reference to the price level.

The meeting adjourned at 5:45 o'clock, with the understanding that the Open Market Investment Committee would submit its final report to the Federal Reserve Board later on in the week.

* * * * * * *

The Open Market Investment Committee reconvened on Wednesday afternoon, May 11, 1927, at 12:30 o'clock.

Present:

Governor Strong, Chairman
Governors Harding, Norris, McDougal
and Fancher
Mr. Harrison, Acting Secretary

The committee considered a draft of report prepared by the committee at lunch on Tuesday, May 10, as modified by the chairman on Wednesday morning before the meeting. Upon consideration, it was

VOTED to approve the report as amended, and the secretary was requested to have it retyped, with the understanding that the preliminary memorandum as finally revised should be mimeographed to be substituted for the first draft distributed among the committee and the members of the Federal Reserve Board on May 9. The preliminary memorandum as revised May 11 is attached hereto. The report of the committee as finally approved by the committee and the Governors Conference is as follows:

"The Open Market Committee, after considering the attached memorandum, and after discussion with the Federal Reserve Board, submits the following recommendations of policy for the period ending August 1 next:

"(1) That no further sales of System securities be made in order to offset arrivals of gold from abroad now known or anticipated.

"(2) That it shall be the policy of the committee between now and August 1 next, gradually to acquire, if possible to do so without undue effect upon the money market, sufficient additional short-time government obligations to bring the total of the committee's investment account up to $250,000,000. In interpreting the expression 'undue effect upon the money market,' the committee would expect to keep in mind any changes which might occur in the general level of money rates, as well as the extent to which these purchases might effect a reduction in the amount of borrowings by member banks.

"While this policy is not directed towards bringing about a reduction in discount rates by any Federal reserve bank, nor is that immediately anticipated, it is recognized that some lowering of market rates for money might nevertheless justify such a reduction later in the year, especially at the principal financial centers. The recommendation in paragraph two is also made after consideration of the fact that somewhat lower interest rates ordinarily operate to check gold imports; in fact, that was one of the effects of purchases of securities made in 1924.

"The committee further expects to continue studies of those methods set out in the preliminary memorandum by which increases in the System's portfolio might be brought about without increasing the amount of Federal reserve credit in the market. It expects to discuss with the Treasury Department those methods with which the Treasury is concerned, and requests that the Federal Reserve Board give consideration to those particular items, such as reserves on time deposits, which relate to the regulations of the Federal Reserve Board."

Meeting of the Open Market Investment Committee
with the Federal Reserve Board
10:30 Thursday morning, May 12

Present:

Honorable A. W. Mellon, Chairman
Governor Crissinger, and Messrs. Platt,
Hamlin, Miller, James, Cunningham,
McIntosh of the Federal Reserve Board
Governors Strong, Harding, Norris, McDougal,
Fancher
Mr. Harrison, Acting Secretary
Dr. Goldenweiser and Mr. Eddy

The Acting Secretary distributed copies of the report of the Open Market Investment Committee dated May 11, together with mimeograph copy of the preliminary memorandum relative to open market policies dated May 9, 1927, and revised May 11.

After each member of the Board had had opportunity to read the report, Governor Strong explained that the report had been prepared by the committee, after thorough consideration of all the factors referred to in the preliminary memorandum, with a view to outlining a policy for the next few months for approval by the Board and the committee, with the understanding that the responsibility for the execution of the recommendations would rest with the committee. He also explained that the report had been studied by the Governors' Conference and that it was unanimously approved by that conference. After a thorough discussion of the report concerning which various views were expressed by the different members of the Board, Mr. Hamlin made a motion that the report be approved. Before action was taken on this motion, Dr. Miller moved as a substitute that the report be received and made a special order for some later time to be fixed by Secretary Mellon and Governor Crissinger. After discussion this substitute motion was passed and the meeting adjourned at 12:10 o'clock p. m.

George L. Harrison,
Acting Secretary.

Meeting of the Open Market Investment Committee
with the Federal Reserve Board
10:30 Thursday morning, May 12

Present:

Honorable A. W. Mellon, Chairman
Governor Crissinger, and Messrs. Platt,
Hamlin, Miller, James, Cunningham,
McIntosh of the Federal Reserve Board
Governors Strong, Harding, Norris, McDougal,
Fancher
Mr. Harrison, Acting Secretary
Dr. Goldenweiser and Mr. Eddy

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George L. Harrison,
Acting Secretary.

May 9, 1927.
Revised copy May 11.

PRELIMINARY MEMORANDUM RELATIVE TO OPEN MARKET POLICY

The principal transactions in the Special Investment Account since the last Governors Conference were reviewed in the chairman's report to the committee on March 21, and copies of this report were sent to all Governors. In accordance with the action taken at that meeting, purchases of 25 million dollars of securities were made in the market to replace March 15 maturities, and the Special Investment Account was thus restored to 200 million dollars, which is approximately the same amount as has been maintained for the past two years. Recent transactions resulting from large purchases of gold, are described hereafter.

General Credit Situation

For many months business has been active and has continued to maintain, and in some directions even to exceed, the rate of production and consumption of immediately preceding years, although a number of recent developments have been of a character which might have had a widespread unfavorable effect had the general business and financial situation not been fundamentally sound. These developments are, of course, the extensive floods in the lower Mississippi Valley, some overproduction and price declines in the oil industry, disturbing financial developments in Japan, reduced production and consequently reduced working time for labor in two or three large automobile concerns, and not so recently the collapse of a number of real estate and building speculations and of one or two large installment finance companies.

The total volume of credit in use, estimated from the reports of the reporting member banks, is now about a billion and a half dollars larger than a year ago. The considerable expansion of the last two months has been distributed between increases in commercial loans, security loans and investments. On the other hand, the total amount of credit extended by the Reserve banks is about one hundred million dollars less than this time last year. As the net gold imports (excluding the movement now under way) within this period were about 105 millions, the reduction of Reserve bank credit has about offset gold imports.

The figures for Reserve System earning assets are as follows:

(in millions)

	April 27,1927	April 28,1926.
Bills discounted - - - - - - - - - - - - -	444	514
Bills bought in open market - - - - - - -	242	199
U. S. Securities - - - - - - - - - - - - -	318	389
Total bills and securities - - - - - - -	1006	1114

While total discounts at the Reserve banks are smaller than a year ago, the difference is largely due to reduced borrowings by country banks as reporting banks in principal centers are borrowing nearly as much as they did a year ago. Money rates are about 1/2 per cent. above this time last year, as shown by the following table. The present tendency is for higher rates than last year. For example, time money is 3/8 higher than last year, 90-day bills are 1/2 higher, and Treasury certificates and notes show an even larger increase. The New York discount rate is 1/2 per cent. higher.

Money rates at New York

	April 28, 1927	April 28, 1926
Call money - - - - - - - - - - - - - - - - -	* 4	* 3 1/2
Time money - 90-day - - - - - - - - - - - - -	4 3/8	4
Prime commercial paper - - - - - - - - - - -	4-4 1/4	4 4 1/4
Bills - 90-day unendorsed - - - - - - - - - -	3 5/8	3 1/8
Treasury certificates and notes -		
maturing June 15 - - - - - - - - - -	3.46	2.51
maturing September 15 - - - - - - -	3.51	3.07
Federal Reserve Bank of New York -		
rediscount rate - - - - - - - - - -	4	3 1/2
Federal Reserve Bank of New York -		
buying rate for 90-day bills - - -	3 3/4	3 1/2

* Prevailing rate for preceding week.

A review of the general credit situation, of rates and business, brings out the following striking facts:

(1) That the general level of interest rates in New York, where changes of rates generally originate, is about 1/2 of one per cent. above last year, the discount rate of the Federal reserve bank also being 1/2 of one per cent. higher.

(2) The amount of bank credit employed for conducting the country's business, at a volume certainly much above the average of the last few years, is only $1,500,000,000 above what it was last year.

(3) While irregularly distributed between the classes of goods, the general level of commodity prices has experienced a considerable fall, and over the greater part of the past year the decline in prices has been in both agricultural and non-agricultural commodities. Considering the reluctance of member banks to borrow from the Reserve banks, coupled with the considerable decline in interest rates which is occurring in Europe, the question is raised as to whether the somewhat greater restraint now being applied to the extension of credit at the money center (New York), coupled with the reduction of the total of the open market investment account over the past 18 months or two years from $500,000,000 to less than $200,000,000, has not gradually had the effect of exercising some pressure, imperceptible in any change over a short period, but now becoming apparent when examined as to its effects over a longer period.

Gold Movements

Between January 1 and May 1 of this year, gold imports into the United States have amounted to about $110,000,000, including $8,000,000 from Japan, and exports during the same period were $26,000,000. Net imports during this period were therefore $84,000,000. Inasmuch as approximately $14,000,000 of the gold exported was gold which had been earmarked before the period under discussion, about $98,000,000 was the net amount added to the monetary gold supply of the country during the first four months of the year. This gold movement, together with the imports of 1926, account largely for the fact that the System's earning assets show a decline during the past year, in spite of an increase of some billion and a half dollars in bank credit.

Entirely apart from the movement of gold referred to above, there have been some significant developments since May 1, not included in the above figures. During the last part of April, the Bank of France recovered approximately $90,000,000 of gold from the Bank of England by the repayment of its credit to the Bank of England. Of this $90,000,000, $12,000,000 arrived in New York last week, $18,000,000 is still on the water, and $60,000,000 was purchased by the Federal Reserve Bank of New York on May 6 and is now held by the Bank of England under earmark for account of the New York bank. In addition to this Bank of France gold, $2,500,000 has recently been imported from Australia, and another $2,500,000 more is now on the water from Australia and expected to arrive in this country this week.

A somewhat disturbing factor arose in the probability of the importation and sale to the Federal Reserve Bank of New York of the $90,000,000 of gold, negotiations for the purchase of which had been concluded by one of the New York member banks from the Bank of France. It was learned that space had been reserved on the steamers and arrangements had been made for shipping the entire amount of gold; in fact, one shipment was about to arrive in New York, and others were being loaded. In view of this situation, after consulting with all the members of the Open Market Investment Committee and with the Federal Reserve Board by telephone, it was arranged to purchase from the Bank of France all of the gold - nearly $60,000,000 - which had not been shipped, and to sell the

Bank of France a like amount of the September maturity of certificates of indebtedness held in the Open Market Investment account. By this arrangement, the money market status remained unchanged, except as to the gold which had already been shipped, leaving the committee in position to determine later at its meeting whether these securities should be replaced or not. Securities were sold to offset $9,000,000 of the $12,000,000 already arrived, but no arrangements have been made for sales to offset the balance of the gold which will arrive from London and from Australia, amounting in all to about $20,000,000. With the sale already made and further sales, if made to offset further gold arrivals, the securities remaining in the System's portfolio account will be a little over $100,000,000, too small an amount to afford security against possible future developments. This will be appreciated, for example, if the $90,000,000 now purchased had arrived at a time when we had no portfolio of government securities available. It is clear, therefore, that the committee must from now on give careful attention to meeting this gold problem, either by increasing its portfolio in anticipation of future developments, or by adopting other measures. The method of doing so should be determined with regard to whether the time has or has not arrived when the Federal Reserve System can afford to put new funds in the market, the effect of which would be to reduce the borrowings of member banks, principally in New York, and possibly to reduce the System's holdings of bills. There are various possibilities for dealing with the gold problem as a whole which have never heretofore been discussed in the committee's report and which are now submitted simply for discussion. None of them are recommended at this time, but are intended simply as a summary of all possibilities. They are:

(1) The committee could replace the securities sold to the Bank of France. The immediate effect would be to reduce the amount of member

bank borrowings in New York, which are now running on the average at from $100,000,000 to $150,000,000.

(2) Those Federal reserve banks which have considerable holdings of long time bonds could dispose of those bonds, realize their profit and repurchase through the committee as a part of the committee's account, an equivalent amount of short time securities. These, with other short term government securities owned by individual Reserve banks, could be added to the System holdings without reducing the total earning assets of the individual Reserve banks, and thus increase the committee's account to over $200,000,000.

(3) Arrangements might be made with the Secretary of the Treasury for somewhat increasing balances carried with the Federal reserve banks, and reducing the amount carried with special depository banks.

(4) Some or all of the $75,000,000 of 2 per cent. Panama Canal bonds could be called and the national bank notes issued against them retired. Further purchases of the 2 per cent. Consols of 1930 could be made in anticipation of their possible retirement in 1930, as contemplated by the Secretary of the Treasury in his report of 1924.

(5) By gradual stages, or all at once, the time schedule of the Par Collection System could be adjusted so as to increase the volume of uncollected checks and correspondingly reduce the reserve of members.

(6) Plans could be undertaken for retiring the greenbacks, which however would require legislation.

(7) Further amounts of the capital of the Federal reserve banks could be called.

(8) The reclassification of reserve cities could be gradually undertaken so as to increase reserve requirements.

(9) A readjustment of the relations of the Reserve banks to the market for gold could be effected if the Secretary of the Treasury saw fit

as authorized by law, to discontinue paying cash up to 98 per cent. of the value of imported gold, thus throwing the market for gold entirely upon the Federal reserve banks and enabling them to reduce the gold point for imported gold by the equivalent of a loss of interest for the period during which payment would be delayed. By reason of our Treasury practice, the United States is today paying the highest price of any world market for gold.

(10) The Federal Reserve Board, of course, after adequate study, could revise the definition of what constitutes a time deposit, thus raising the reserve requirements. This is probably justified by the fact that something like 60 per cent. of the increase in bank deposits in the United States over the past ten years consists of that class of deposits which require only 3 per cent. reserve.

(11) A revision of the regulations of the Federal Reserve Board in relation to the maintenance of reserves, by averaging reserves for a period of a week in Federal reserve bank cities, and two weeks in the rest of the country, could have the practical effect of somewhat increasing the amount which member banks must borrow.

(12) The Federal Reserve Board could revise its ruling relative to currency in transit, which in effect reduces reserve requirements in those districts where the ruling is now applied.

The above comprehend most, if not all, of the possible measures available for dealing with the problem of gold imports in view of our reduced portfolio. They are submitted for consideration and study.

The possibility of gold imports must not be overlooked, and may indeed be imminent. The underlying causes of such a movement would be:

(1) The continued maintenance of our present level of interest

rates, somewhat higher than a year ago, in the face of declining interest rates and reducing bank rates in Europe.

(2) The fact that our technical practice in dealing with gold makes this the best market in which to sell it and one of the most difficult from which to export it.

(3) The possibility, regarded by some as the probability, that within the next two years Germany will be forced to ship us large amounts of gold in order to meet reparation payments in the standard year.

(4) Heavy foreign payments to meet the service on all foreign loans.

Nor must the possibility be overlooked that conditions may change rapidly and instead of experiencing a large addition to our gold reserve, there is indeed a possibility, although more remote, that within the next few years we may sustain a large loss of gold.

Gold exports from this country can arise from two causes:

(1) The first is the perfectly normal movement resulting from exchange rates reaching a level at which it is cheaper to make payments abroad by shipping gold than by buying exchange.

(2) The other, however, can occur irrespective of the gold shipping point, because of large balances held in this country for account of foreign governments and foreign banks of issue, which, as in the case of Germany, may decide to take gold for reserve purposes, irrespective of the gold point.

No danger need bp apprehended as to a normal export of gold, but we might sustain a large loss of gold under the second category at any time, and that we are now prepared to deal with successfully because of the large proportion of such balances held by the Federal reserve bank, the export of which could easily be provided for by our purchasing the securities now held for account of our foreign correspondents. The only embarrassment likely to occur as a result of such a demand will be due to the lack of an adequate supply of American gold coin, concerning which discussion has been had from time to time with the Treasury.

Looking, therefore, to the future, that is, say for the next three years, the committee is of the opinion that the policy of the Federal Reserve System should be to prepare itself to deal with either a large import movement of gold or a large export movement of gold. Any other position would expose the System to the charge of lack of foresight.

In view of the many alternatives to be considered, and especially in view of the fact that whatever may be the policy of the System it will involve taking a definite position as to the money market, the committee prefers to defer any recommendation until after discussion with the Federal Reserve Board and a definite expression of their views.

C O P Y

FEDERAL RESERVE BOARD

WASHINGTON

May 13, 1927.

Dear Governor Strong:

At the meeting of the Federal Reserve Board this morning, consideration was given to the report of the Open Market Investment Committee, dated May 11, 1927, in which the Committee recommended: "(1) That no further sales of System securities be made in order to offset arrivals of gold from abroad now known or anticipated" and "(2) That it shall be the policy of the committee between now and August 1 next, gradually to acquire, if possible to do so without undue effect upon the money market, sufficient additional short-time government obligations to bring the total of the committee's investment account up to $250,000,000. In interpreting the expression 'undue effect upon the money market,' the committee would expect to keep in mind any changes which might occur in the general level of money rates, as well as the extent to which these purchases might effect a reduction in the amount of borrowings by member banks."

The Board voted to approve the report and recommendations contained therein, with the feeling that the securities proposed to be purchased should be accumulated slowly and with a view to the possibility that it may not be advisable to purchase the full amount authorized within the period of time mentioned.

Very truly yours,

(Signed) D. R. Crissinger,

Governor.

Mr. Benjamin Strong, Chairman,
Open Market Investment Committee,
c/o Federal Reserve Bank,
New York, N. Y.

CONFIDENTIAL

Minutes of meeting of the Open Market Investment Committee for the Federal Reserve System in Washington on July 27, 1927 at 11:00 a. m.

PRESENT: Messrs. Crissinger, Platt, Hamlin, James and McIntosh
Members of the Federal Reserve Board

Governors Strong, Harding, Norris, Fancher and McDougal
Members of the Open Market Investment Committee

Governor Young, Federal Reserve Bank of Minneapolis
Governor Biggs and Chairman Martin, Federal Reserve Bank of St. Louis
Mr. Harrison, Deputy Governor, Federal Reserve Bank of New York
Mr. Mills, Undersecretary of the Treasury
Mr. Burgess, Acting Secretary, Open Market Investment Committee
Messrs. Noell and McClelland, Assistant Secretaries, Federal Reserve Board

The meeting was called as a meeting of the Open Market Investment Committee with the Federal Reserve Board and representatives of two of the midwestern banks were present. The Chairman presented his report reviewing open market operations and credit conditions. The credit policy of the System was thereupon fully discussed.

Consideration was given to the continued fall in commodity prices, to the fact that there was a diminution of borrowing from the reserve banks due apparently to some slackening in business, and especially to the relation of money rates in the United States to money rates in Europe. It was reported that because of heavy foreign payments which are likely to increase with the fall movement of commodities to Europe, there was a continued drain on European central bank gold reserves, which made it more than likely that central bank rates in Europe would need to be further advanced this fall. The German and Austrian rates have already been once advanced and there is some probability of a one per cent advance in the rate of the Bank of England.

All present at the meeting recognized that these developments would necessarily have a depressing effect upon business abroad and might tend to restrict the freedom of purchases of goods in this country at the usual season. It was also brought out that it is the duty of the central banks to keep money rates at as low a level as may be attained with safety, and that at this time rates could be reduced not only without harm but with reasonable expectations of beneficial results. It was felt that the only possible adverse development resulting from a general lowering of discount rates would be in the speculative security markets, but that this possibility should not stand in the way of the execution of an otherwise desirable policy.

There was no exception to the view that the time has arrived, or was approaching, when the discount rate in New York should be reduced, and with one or two exceptions there was no dissent from the view that a System policy of lower discount rates should in general prevail. It was pointed out, however, that local conditions in some of the interior reserve districts did not indicate any demand for rate reductions in those districts and that the small borrowings from the reserve banks indicate an adequate supply of credit for all needs at the present rates. Officers of some of the larger member banks were quoted as opposed to rate reductions. On the other hand, it was pointed out that reductions now, which would result in no harm and considerable possible benefit, would place the reserve banks in position to make increases later which might serve as warnings without penalizing business with high rates.

It was also suggested that in order to make a three and one-half per cent discount rate effective some further purchases of securities might be desirable up to say $50,000,000.

The most important consideration at the meeting was undoubtedly the fact that the differential between the rates in New York and the rates in London was not to-day sufficient to enable London, and therefore the rest of Europe, to avoid general advances in rates this autumn unless rates here were lowered, and that the consequence of such high rates as would result in Europe would be unfavorable to the marketing of our export produce abroad and would have an adverse effect generally on world trade.

Before adjournment of the meeting, the foregoing portion of these minutes was read to the meeting and adopted without objection. Thereupon, upon motion of the members of the Federal Reserve Board present voted that the authority of the Open Market Investment Committee be extended for the purchase, as and when conditions warrant, of not to exceed an additional $50,000,000 of investments.

(Signed) W. R. Burgess, Acting Secretary
Open Market Investment Committee

CONFIDENTIAL July 27, 1927.

PRELIMINARY MEMORANDUM RELATIVE TO OPEN MARKET POLICY

The gold movements of the past two months have illustrated the need for preparedness on the part of the Federal Reserve System to deal with either gold exports or imports, which was emphasized in the Chairman's memorandum discussed at the last Governors' Conference. This year's gold movements have included the import of 130 million dollars of gold from abroad, the purchase of 62 million dollars abroad, the sale of 100 million dollars for earmarking here, and the resale of 60 million abroad. There has thus been an import movement, or its equivalent, of 190 million dollars and an export movement, or its equivalent, of 160 million dollars. Fortunately these two movements have largely offset each other in their influence on the domestic credit situation. Otherwise they might have occasioned embarrassment. These movements were largely unforeseen and unforeseeable, although at any time possible under present conditions.

Recent transactions in the special investment account have been largely for the purpose of dealing with these changes in gold. At one time, in May, the account was as low as 136 million dollars, and it has now been restored to 265 million dollars. The increase represents largely purchases to offset the earmarking of 100 million dollars of gold here, but includes in addition the purchase of about 30 million dollars of securities under the authority arranged at the time of the Governors' Conference. The following figures show the changes from week to week in the special investment account. It would appear that this portfolio should be increased from time to time when favorable opportunity offers, if the system is to be in a position to meet future extraordinary gold movements.

April	27 - - - - -	$201 millions
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A temporary increase in the account in ordinary course may be involved in replacing 56 million of maturities in September which includes 30 million taken over from a foreign account in exchange for March certificates. It may be necessary to take over further amounts of securities from foreign correspondents.

The Credit Situation

A number of important changes have taken place in the domestic and foreign credit situation since the Governors' Conference. These may be summarized as follows:

1. Money rates abroad have risen vigorously; open market money rates in London, Berlin, Zurich, and a number of other centers are markedly higher than they were three months ago. The Reichsbank and the Bank of Austria have raised their discount rates. Open market money rates are close to or above the bank rate in London, Berlin, Zurich, Amsterdam, and Milan, as shown in an attached table. These firmer money conditions are undoubtedly exerting continuing pressure upon world trade and world prices, which is liable to react unfavorably upon our own trade and prices.

2. There has been some reduction in business activity in this country, not serious, but indicating a spirit of great caution in business.

3. There has been some congestion of the bond market, due largely to undigested new issues. This situation has been partially corrected.

4. Due largely to reduced industrial payrolls there has been

a slight reduction in the past few weeks in the credit and currency demand, and total bills and securities of the Reserve System have dipped below one billion dollars. The New York Reserve Bank gained 50 million last week in transfers from the interior and New York City member bank borrowing was correspondingly reduced.

5. There is growing ease in money conditions, although some rates are still slightly higher than a year ago, due probably to a higher discount rate at the New York Reserve Bank. Current quotations for money are as follows compared with last year.

	A Year Ago	July 23, 1927
Call money	4	3 3/4
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90-day bills	3 3/8	3 1/2
Treasury Issues		
Dec. maturity (notes)	3.03	2.87
Mar. " (C of I)	3.31	3.19
Discount Rate N.Y. F.R.B.	3 1/2	4

The Prospect for Autumn

Normally the approaching seasonal demand for funds might be expected to tighten money conditions somewhat. If this takes place it would have the result (1) of increasing the pressure on world money markets and perhaps forcing up the Bank of England discount rate, and certain of the Continental discount rates, with consequent unfavorable reaction upon world trade and prices; (2) of accentuating the existing tendency towards some reduction in business activity.

If on the other hand steps should be taken which would prevent any seasonal increase in money rates, and tend rather towards somewhat easier money conditions, the following results might be anticipated:

1. An easing of the pressure upon world money markets, which would react favorably upon world trade. The results would be felt partly through the tendency for balances to move in the direction of the highest rate, and partly as lower bill rates here would attract financing to our bill market which might otherwise go to

London and require funds there.

2. Coming at the crop moving season easier money conditions would tend to facilitate the marketing of the crops at favorable prices.

3. It would tend to remove any credit pressure which may now be exerted upon business, and would encourage business enterprise.

4. There would on the other hand be danger that easier money might encourage speculation. The spirit of business is so cautious that it seems doubtful whether speculative tendencies in business would easily arise, but it is probable that easier money would stimulate speculation in securities.

If under these circumstances it should seem wise to follow a policy favoring easier money conditions, the immediate problems would be (1) to localize the effects of easier money conditions, where they would be most beneficial; and (2) to prevent excessive speculation or excessive growth in the volume of credit.

In this connection the attached table shows the total bills discounted at Federal Reserve Banks in the 12 districts. The total is nearly 100 million smaller than it was a year ago and the decreases in bills discounted exceed 25 per cent in the New York, Richmond, Minneapolis, Kansas City, and Dallas districts.

Total Bills Discounted by Federal Reserve Banks
(in millions of dollars)

	Week Ended	
	July 21, 1926	July 20, 1927
Boston	24	32
New York	126	87
Philadelphia	44	42
Cleveland	35	28
Richmond	43	19
Atlanta	44	37
Chicago	56	55
St. Louis	35	33
Minneapolis	8	6
Kansas City	17	11
Dallas	18	8
San Francisco	45	45
Total	495	403

Money Rates in World Markets

		July 1926	May 1927	July 1927
London	- Market Rate	4.25	3.69	4.31
	Discount Rate	5	4.5	4.5
Berlin	- Market Rate	4.5	4.88	5.88
	Discount Rate	6	5	6
Paris	- Market Rate	6	2.25	2.13
	Discount Rate	6	5	5
Amsterdam	- Market Rate	2.76	3.5	3.5
	Discount Rate	3.5	3.5	3.5
Brussels	- Market Rate	6.70	4.25	3.75
	Discount Rate	7	5.5	5
Zurich	- Market Rate	2.31	3.13	3.81
	Discount Rate	3.5	3.5	3.5
Milan	- Market Rate	8.5	9.25	8
	Discount Rate	7	7	7
Vienna	- Market Rate	6	5.38	5.75
	Discount Rate	7.5	6	7
New York	- Bill Rate	3 3/8	3 5/8	3 1/2
	Discount Rate	3 1/2	4	4

C O N F I D E N T I A L (2)

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3. It would tend to remove any credit pressure which may now be exerted upon business, and would encourage business enterprise.

4. There would on the other hand be danger that easier money might encourage speculation. The spirit of business is so cautious that it seems doubtful whether speculative tendencies in business would easily arise, but it is probable that easier money would stimulate speculation in securities.

If under these circumstances it should seem wise to follow a policy favoring easier money conditions, the immediate problems would be (1) to localize the effects of easier money conditions, where they would be most beneficial; and (2) to prevent excessive speculation or excessive growth in the volume of credit.

In this connection the attached table shows the total bills discounted at Federal Reserve Banks in the 12 districts. The total is nearly 100 million smaller than it was a year ago and the decreases in bills discounted exceed 25 per cent in the New York, Richmond, Minneapolis, Kansas City, and Dallas districts.

Total Bills Discounted by Federal Reserve Banks
(in millions of dollars)

	Week Ended	
	July 21, 1926	July 20, 1927
Boston	24	32
New York	126	87
Philadelphia	44	42
Cleveland	35	28
Richmond	43	19
Atlanta	44	37
Chicago	56	55
St. Louis	35	33
Minneapolis	8	6
Kansas City	17	11
Dallas	18	8
San Francisco	45	45
Total	495	403

Money Rates in World Markets

		July 1926	May 1927	July 1927
London	- Market Rate	4.25	3.69	4.31
	Discount Rate	5	4.5	4.5
Berlin	- Market Rate	4.5	4.88	5.88
	Discount Rate	6	5	6
Paris	- Market Rate	6	2.25	2.13
	Discount Rate	6	5	5
Amsterdam	- Market Rate	2.76	3.5	3.5
	Discount Rate	3.5	3.5	3.5
Brussels	- Market Rate	6.70	4.25	3.75
	Discount Rate	7	5.5	5
Zurich	- Market Rate	2.31	3.13	3.81
	Discount Rate	3.5	3.5	3.5
Milan	- Market Rate	8.5	9.25	8
	Discount Rate	7	7	7
Vienna	- Market Rate	6	5.38	5.75
	Discount Rate	7.5	6	7
New York	- Bill Rate	3 3/8	3 5/8	3 1/2
	Discount Rate	3 1/2	4	4

(D)

Correspondence w/ Phila. &
Chicago FR Banks
RE: discount rates

CONFIDENTIAL:

August 18, 1927

My dear Norris:

You will I am sure agree that I have been scrupulously careful in not intruding my own views upon other reserve banks in rate matters, nor in fact in any other local affairs except those in which we are all concerned as a system. On the other hand, I have always felt that the New York rate had a great bearing upon the rate policy of other reserve banks, as well as a definite reaction upon their local conditions and so have never hesitated to invite discussion of proposed changes in our rate with my colleagues in other reserve banks. It does develop this time, however, that policies as to rates in some of the other reserve cities, especially Boston, Philadelphia and Chicago, now have a considerable effect upon the New York position, and it is for that reason that I am writing you.

When we reduced our discount rate to 3-1/2% and as the result of that action (and of open market purchases) the general level of rates for more liquid loans in New York declined, there soon developed a tendency to withdraw funds from New York; - not only funds which are loaned here, but balances which are carried in bank. I believe that tendency has now reached a point where demands upon us for accommodation by our members are somewhat larger than they would be were both Philadelphia and Chicago to reduce their rates to 3-1/2%. That, however, is a matter for you and your directors to judge and decide. The important considerations for our present policy I think we discussed quite fully in Washington. We also invited the Open Market Committee to New York so as to discuss the matter first hand with our foreign visitors.

This is the season of the year when we export the great bulk of our raw materials, principally produced on the farms. Payment in dollars for these exports puts a heavy strain upon the exchange market. Prior to our rate reduction most of the European exchanges were hovering around the point where gold could be profitably exported to this country; some gold was coming here, and more would have come had we not been able to purchase and hold gold in London, and by good fortune resell it. We were either directly advised or had other reason to believe that if we did not reduce our rate bank rates in Europe would have to advance. Since our rate reduction was announced, I have advice directly from Europe that at least three or four of the principal banks of issue which were then considering rate advances now feel that they can at least postpone and possibly escape doing so.

Of course the reduction in our rate is only effective if it is reflected likewise in market rates. Not only has our action for the present been successful as to rates of discount at the banks of issue, but it has resulted in strengthening sterling exchange to a point where we have been able to liquidate about $12,000,000 of our balances in the Bank of England, and we are hopeful that we will be able to effect further reduction from time to time without impounding gold in London. But we may have difficulty still if any unnecessary drain on New York continues from out of town.

Now it seemed to me that this situation, upon which so much depends for this country, is a thorough justification of our rate policy, irrespective of any effect which our action might have upon stock speculation. That ogre will always be with us and if the Federal Reserve System is to be run solely with a view to regulating stock speculation instead of being devoted to the interests of the industry and commerce of the country, then its policy will degenerate simply to regulating the affairs of gamblers. I have no hesitation in expressing my impatience with such a view of our role.

I am wondering whether you and your colleagues feel as I do in regard to the importance of this policy and realize that the position of your institution and that of Chicago as well has a direct bearing upon the success of what we are undertaking to do. I am not writing to suggest, much less urge, that my own views should be adopted in Philadelphia, but rather to invite from you some explanation, if you feel willing to give it, of the contrary views which apparently your associates hold. I think such an exchange of views would be of use to both of us. At any rate please write me quite frankly and fully.

Best regards,

Sincerely yours,

George W. Norris, Esq.,
Governor, Federal Reserve Bank of Philadelphia,
Philadelphia, Pa.

Extra copy

CONFIDENTIAL:

August 18, 1927.

My dear McDougal:

To save writing two letters, I m enclosing copy of one which I have just sent to Norris. Without aid from you and him we may have q quite a struggle to keep our money market in order through the next few months. The penalty for failure to carry through our program successfully will be higher bank rates in Europe, considerable depression of the foreign exchanges, and, I am sorry to most reluctantly admit, that I think it will have a very adverse effect upon our ability to market abroad what we produce and must sell there.

This is really the whole story, and I am wondering whether you will not send me a reply to the inquiry contained in my letter to Norris just as you would express it orally if you were here in New York.

Best regards,

Sincerely yours,

J. B. McDougal, Esq.,
Governor, Federal Reserve Bank of Chicago,
Chicago, Illinois.

Extra Copy

PERSONAL AND CONFIDENTIAL.

August 22, 1927.

Dear Mr. Hutt:

Your personal and confidential letter of August 20, addressed to Governor Strong, was received here this morning. Governor Strong is spending a day or two out of town and will not return until Wednesday, at which time your letter will be brought to his attention.

I note with interest the report you make of the consideration given the rate subject by your directors on August 5 and subsequent dates; but, in view of the importance of the subject mentioned in Governor Strong's letter, I am strongly inclined to the belief that he would like to have it forwarded to Governor Norris for his consideration. I, too, am in sympathy with the idea of not bringing business matters to the attention of the governor when he is away on holiday, but I do think that this matter is of sufficient importance for the letter to be forwarded to Governor Norris.

With kindest regards, I am,

Sincerely yours,

J. H. CASE,
Deputy Governor.

Mr. Wm. H. Hutt,
Deputy Governor, Federal Reserve Bank
of Philadelphia,
Philadelphia, Pennsylvania.

Extra Copy

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August 22, 1927.

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With kindest regards, I am,

Sincerely yours,

J. H. CASE,
Deputy Governor.

Mr. Wm. H. Hutt,
Deputy Governor, Federal Reserve Bank
of Philadelphia,
Philadelphia, Pennsylvania.

FEDERAL RESERVE BANK OF CHICAGO

August 24, 1927.

Ack 8/26/27

PERSONAL AND CONFIDENTIAL.

Mr. Benj. Strong, Governor,
Federal Reserve Bank of New York,
New York, New York.

Dear Governor Strong:

I have today returned from a short vacation up North, and find awaiting your letter of the 18th instant, with which there was enclosed a copy of your letter to Governor Norris, intended also for Chicago, inviting an expression of our views with respect to the question of discount rate adjustments.

Ensuing on the meeting of the Open Market Investment Committee, held in New York in July, I reported as fully as possible to our Board, making particular reference to the views expressed there bearing upon the discount rate policy of the Federal Reserve System and its relation to, and its effect upon, the discount rates of London and the central banks in Europe. Later on, following the meeting of the Open Market Investment Committee held in Washington on July 27th, I informed our Executive Committee of the developments there, and, of course, this report included the presentation of the minute of that meeting, as prepared for submission to the Boards of Directors of all of the Federal Reserve Banks. Consequently, my associates are informed with respect to the underlying considerations which prompted your action in the matter of rate adjustment. I think the important features involved have been carefully considered here. There appears to be nothing in the local situation here or in the district situation which would justify a change in our rate. It is understood that the governing factor in the matter of your rate reduction, and, I believe, in the changes made by other banks, is the international situation, and it seems to me that the desired result has already been attained through the reduction in your rate.

With respect to the question of making the rate a System matter, up to the present time we are not convinced as to the necessity of having a uniform rate in all districts.

While I understand from your letter that you hold a contrary view, it seems to me that action here would have little, if any, effect upon the New York position. It seems from your letter that you are of the opinion that failure on our part and on the part of Philadelphia to act has resulted in a tendency to withdraw funds from New York. As a result of inquiry made locally, we do not find that funds are being withdrawn from New York to Chicago. On the other hand, however, we know that banks in this district are transferring funds to London because of the higher rate obtainable there, and this, according to my understanding, is a natural result of the establishment of a larger differential as between your rate and the London rate.

In the foregoing, I have endeavored to inform you with respect to our position in the premises, and I can assure you that we will continue to watch the situation closely and be prepared to act if and when, in our judgment, it seems expedient to do so.

Very truly yours,

J B McDougal

Governor.

K

Extra Copy (4)

PERSONAL AND
CONFIDENTIAL

August 26, 1927.

My dear Mac:

I have read that austere letter of yours dated August 24, and after finishing it feel as though I were sitting in an unheated church in midwinter, somewhere in Alaska. The fact is, my dear Mac, as I explained to you in Washington I don't believe, and never have belieged that local conditions in Chicago would be justification alone for a reduction in your rate. Nor do I believe that simply local and domestic conditions in New York were justification for our rate reduction. But what I do believe is that the objects which we sought to accomplish by our rate reduction are mainly for the benefit of the producers of exportable crops in your district and the other districts, and that their ability to find their markets for the surplus of their crops in Europe is very much advanced by what we have done and would be further advanced if you followed with a similar rate reduction. In other words, it is neither a New York question nor a Chicago question nor a district question, but a national question bearing upon our markets in Europe, consequently an international question., And it was solely on that account that I felt justified in writing you, and the fact that you and your associates in the bank take the position that there is no justification in the Chicago district for reducing the discount rates strikes me as similar to a statement that there is no justification for anybody wearing any clothes when the weather is warm. We don't wear clothes simply to keep warm.

However, I am endeavoring to preserve my sense of humour and want you to cultivate yours. If we don't agree, that ends it, but I am personally sorry that we could not work togbther on a system policy such as this is. It is as much or even more in your interest as a district than it is in ours.

Now, put that in your pipe and smoke it, Old Man, and don't get to think that I have any less regard for you because we disagree now and then.

Sincerely yours,

Mr. James B. McDougal,
C/o Federal Reserve Bank of Chicago,
Chicago, Illinois.

BS/RAH

177

Extra Copy (4)

September 1, 1927.

My dear Norris:

It was kind of you to write me while on holiday. In fact, I felt a little guilty that you should have been troubled by even having to read my letter. What you write me is most illuminating and, if I may say so, most encouraging as to the spirit in which these questions are considered by you and by your associates in Philadelphia.

You have always had very keen appreciation of the importance and the magnitude of this problem of our foreign relations. There are times when it gives us a great deal of anxiety here, and that is especially so whenever there appear to develop sharp deviations of opinion as to our policy.

Beset as we are with a great variety of difficulties in dealing with the personal equations which cannot help but exist in so large and complicated a system as ours, it is encouraging when one of your associates and partners write such a letter as the one I just had from you.

If by chance you are returning home through New York and are able to plan to spend a day here I hope you will do so. If that is not possible you may be able to give up a day after your return and make a visit with us. If so I hope you can do it on the day when our directors meet when we can talk it all over. In any event do not let this matter disturb your vacation. That is really altogether too important.

Sincerely yours,

Mr, George W. Norris,
C/o Sunset Bungalow,
Campobello,
Via Eastport, Maine.

(E)

Cables & Correspondence w/ Foreign Banks of Issue

RE: discount rates

BANK OF FRANCE - PARIS

Confidential Cables

July 28, 1927: Strong to Moreau: (Gov. Bank of France:

One Conditions now seem to justify reducing to 3-1/2 within next fortnight and we expect some interior reserve banks to do so earlier

Two We feel that this is in the general interest as it certainly is for our own position and hope you agree

Three Out look is for further easing of all New York rates

August 4, 1927 Rist (Dept.Gov. Bk of France) to Strong:

One. We note the change looked for in your discount rate which we understand thoroughly. We have discontinued buying gold on London market since July 23rd.

EXTRACT FROM CORRESPONDENCE BETWEEN
FEDERAL RESERVE BANK OF NEW YORK AND BANK OF FRANCE
RE DISCOUNT RATES

August 10, 1927 Governor Strong to Governor Moreau:

"It is only fair that I should also write you something of the motives leading to our recent rate reduction. They can be summarized briefly as follows:

1. There was clearly developing some hesitation in business conditions, not yet widespread but rather spotty as to location and as to the various industries affected, but it nevertheless was becoming apparent that there was some slight slackening of business in various directions.

m 2. We were just entering the season when very heavy demands are made upon our banks for crop moving purposes and when arrangements must be made for financing that portion of the crop which moves to Europe. In view of the business developments it seemed desirable that these demands should be arranged at the least interest cost which was safe, having in view of course the possibilities of speculative developments.

3. The effects of the drag upon foreign bank reserves because of the depressed European exchanges, arising as it did at the commencement of the season when the heaviest payments must be made in this country, convinced us that lower interest rates in this country was the only thing which would overcome this tendency and prevent another large movement of gold to this country.

4. By acting as early as we did the arrangements of credits for the export of our crops was more likely to be made in dollars than in sterling, thereby relieving the exchanges of the immediate demand for dollars which would otherwise arise.

5. The only consideration against a reduction in our rate was the stock market speculation. Personally I was willing to ignore that as a factor as I believed it could not possibly outweigh the importance of the other considerations, and, in fact, I have felt that the advances in stock values and the expansion of the stock loan account had pretty well reached the maximum. Anyway, as it happens, President Coolidge's announcement that he would not run for another term as President, which happened to follow our rate reduction so promptly, has in itself proved to be a check to speculation and I think the danger which we might have apprehended on that score has now been reduced.

"We are now beginning, about a fortnight later than usual, to feel the demand for credit. Our banks are fairly steady borrowers but the position is now such that this necessary financing

August 10, 1927 (continued)

will be conducted smoothly and probably without any advancing interest rates. And we hope that the effect upon the position of the exchanges will be favorable and will continue throughout the fall."

August 19, 1927 Governor Moreau to Governor Strong:

"I appreciate very much the explanation which you so kindly give me of the reasons for your recent discount rate reduction at the Federal Reserve Bank. We understood very well in Paris that you desired to be of help to Mr. Norman. We can only rejoice at any measure that tends to assure the stability of the pound sterling."

August 30, 1927 Governor Strong to Governor Moreau:

"Our rate reduction seems for the present to have accomplished the results desired. We were anxious to avoid further large shipments of gold to this country, and, even more, to postpone or possibly to completely avoid the need for any general advance of bank rates in Europe this fall. I believe such a development would have been distinctly harmful and would have chilled business and business enterprise and interfered with the normal course of economic recovery. Fortunately we have so far escaped anything like an outburst of stock speculation because of this rate reduction and the cheaper money which has accompanied it, but one cannot promise as to the future."

BANK OF ENGLAND - LONDON

Confidential Cables

July 28 — Strong to Norman

ONE — Conditions now seem to justify reducing to 3½ within the next fortnight and we expect some interior reserve banks to do so earlier.

TWO — Please advise me fully of your prospects and whether this may be expected to enable you to avoid advance.

THREE — Outlook is for further easing of all New York rates

FOUR — Am advising Schacht.

July 29 — Norman to Strong

ONE — This is wonderful and you deserve a crown but it is too early for me to answer your paragraph 2.

TWO — Exchange seems stronger for the moment owing to repatriation of proceeds of German loans issued in New York. But the tendency is weak and our prospects must depend on effect to be produced by easing of New York rates and your eventual reduction.

THREE — I doubt being able to give you any useful forecast for at least a month but undoubtedly prospects of our avoiding later advance will be greatly improved by your reduction and this I guess applies also to Schacht.

<u>July 30</u> Harrison to Norman

Our #21 paragraph #1 Kansas City reduced to 3 1/2 last Thursday.

<u>August 2</u> Norman to Strong

ONE Vissering came today to discuss question of increase in his bank-rate to 4 1/2 per cent which he considered imminent - particularly in view of recent exports of gold from Amsterdam to New York. I outlined to him our recent discussion in New York and pointed out easing of your call money rate and reduction in Kansas City with result that he hopes to continue without change. But he is somewhat doubtful how long he can so continue in any event.

TWO Was our 113/27 sufficient for your immediate need.

<u>August 4</u> Federal Reserve Bank of New York to Norman

Our rediscount rate reduced to 3 1/2 per cent effective August 5.

<u>August 8</u> Norman to Strong

ONE Your 30/27 * * * * *

TWO Following your rate reduction there was some temporary easing in discount rates and firm exchanges. Besides supplying continental demands I expect to secure some gold tomorrow for Bank of England and for Federal Reserve Bank of New York in accordance with your #28/27

<u>August 10</u> Federal Reserve Bank of New York to Norman

No. 35/27 Our Discount rate reduction followed by slight further decline in open market money rates;

ninety day time money 4 1/4, prevailing commercial paper rate 4 per cent, bill rates unchanged. * * * * *

EXTRACTS FROM CORRESPONDENCE BETWEEN FEDERAL RESERVE BANK AND BANK OF ENGLAND RE DISCOUNT RATE

<u>August 6, 1927</u> Letter Mr. Lubbock (Dep. Gov. B/E) to Governor Strong:

"The month of July was uneventful here. The market rate of discount remained steady at about 4-5/16: The Bank neither gained nor lost gold: several loans were issued, some of which were not very successful: The exchanges showed a tendency to move against us. The situation was not satisfactory, and we ought to have been gathering strength to meet such demands as may be made on us later in the year.

Last week we received about £400,000 of the South African gold, and your rate was reduced. On this the market were prepared to assume that rates should be easier here, and there was a temporary weakening; but money is not plentiful and the rate has returned to its previous level, where, for the present at any rate, it should remain. The exchanges have moved in our favour, but it is not satisfactory that at this time of the year your exchange should still be below 4.86."

<u>August 16, 1927</u> Letter Governor Strong to Mr. Lubbock:

"I am grateful to you for writing me about the position of affairs in London. Since our rate reduction the exchange position has altered so materially that yesterday we were able to draw on you for £1,000,000 at the minimum rate mentioned in our recent cable exchanges; and it may be that we will liquidate the account still further as opportunity arises from day to day. This I understand is according to the Governor's desire, although, of course, if he would prefer to take advantage of the present opportunity to further reduce the French balances we will not object. The important thing is that we should know precisely your own preference.

The present position has improved and of course the foundation of the improvement is not a very substantial one. Doubtless it is less substantial than it would be had not the French skimmed everything off the market for a time including such loose gold as came to London.

Yesterday I had a call from Mr. Armitage of the Commonwealth Bank and expect later to meet Mr. Mason. Mr. Armitage had a Mr. Collins with him and we had quite a discussion of their plans for opening an office in New York; for placing loans here; and more especially in regard to shipments of gold from Australia. I pointed out to him that were it possible to induce the steamship companies to make reasonable rates to London it would be more satisfactory for us to accept deliveries of gold there at prices which we could afford to buy at rather than to have it come here; and that ultimately arrangements of this sort which would keep gold out of this mouse trap would be to the advantage of everybody, especially the European banks of issue and quite possibly the Bank of England.

August 16, 1927 (continued) Governor Strong to Mr. Lubbock:

"Our money market has not been working quite as easily towards a lower level as we had hoped, largely because of what appears to be a considerable demand for funds in the west, where the crops are now being harvested and which has turned the domestic exchanges adverse to New York and drawn down our gold reserves and impaired New York member banks' reserves. But I still feel that we can handle the situation satisfactorily through the period of fall demand."

August 20, 1927 Governor Norman to Governor Strong:

"Since the reduction in your rate our position has been greatly improved and our control quite satisfactory: this latter is partly due to the markets uncertainties about the Autumn. There is a Government maturity on October 1st of some £80 mil. which will be difficult to deal with except through the short money market: on the other hand one cannot measure the effects of the regular fall payments on the exchanges. But as people seem alive to the dangers perhaps preparations have been made in advance."

August 22, 1927 Governor Norman to Governor Strong:

" "I have no more to say about gold purchases here for your account, I mean other than those to prevent shipments to New York, partly because the question depends upon your willingness to purchase (of which you can judge and I cannot) and partly because the direct shipments from Capetown to Buenos Aires are likely to be so heavy that I doubt whether for some weeks to come there will be any gold in the London Market worth counting. I wrote you the other day how this question struck me and since then you have sold more sterling than I expected.

"In continuation of what I wrote to you on the 11th about the Sterling held by the Bank of France, I can most completely bring you up to date by enclosing a copy of my letter to Rist (to which they entirely agree).

"In so far as I was a party to any understanding, I felt that this position should now be cleared up one way or another. I was committed to Rist as well as to you to do my best and, if it had not been for Moreau's absence, it would have been arranged a couple of weeks ago."

August 25, 1927 Governor Strong to Governor Norman:

"Our rate change seems to have been salutary and effective and none too soon, but we have been scratching a bit to keep the market rates in line with our discount rate. This is partly due to the to the regular seasonal demands and partly due to the reluctance of Philadelphia and Chicago to reduce their rates, which results in some drain from New York to those centers. I think we have lost something like $130,000,000 of our reserves in the last few weeks but I am still without apprehension as to the success of our program and even hope shortly to see these two rates also come down.

******

"Yours of August 11 reached here while I was absent, and has just been read today. I hope all rate advances abroad can be avoided over the fall period. It will be one of the justifica-

August 25, 1927 (continued) Governor Strong to Governor Norman:

tions of our policy which has aroused some slight criticism but nothing disturbing.

*****

"On the whole I think you have done a wise thing in your arrangement with the Bank of France, and I believe the transaction is going through today. It indicates such a willingness on your part to be accommodating and helpful that it will certainly bring an equally satisfactory response from them in later days when new problems arise.

*****

"I think we do see eye to eye in regard to our sterling assets. If the transaction was useful at that moment, that, after all, was what we intended to accomplish, and there is some advantage to us in transferring the London portfolio into a New York portfolio, besides the advantage of having a reserve purchasing power for London bills in case later such purchases become desirable. We would much prefer to buy gold when it will otherwise come to New York, then we can hold it with you and dispose of it as opportunity arises, thereby keeping it out of the mousetrap."

August 29, 1927 Governor Norman to Governor Strong:

"I have been cabling so fully as to the Exchange position that I can say no more about it except that the news of the opening of the Conversion Office (i.e., free gold export) leaves me uncertain as to its probable effect on the Argentine Exchange and on the Argentine demand for gold. It is true that our position may be tender, chiefly because the French skimmed everything off the Market some three months ago: otherwise we should now have been in a strong position. As it is, things are a deal better than a few weeks ago they seemed likely to be."

*****

"Of course I am very anxious that, as we agreed, gold from Australia should be sent to London rather than to New York: I will have the question of freight charges, etc. gone into carefully. But you will remember the answer of the Bank of England to this question while I was in New York: I see it set out in Lubbock's cable of the 18th of last month.

As to gold purchases and prices in general, I now have some hope that the Bank of England will be allowed to pay more than 77s/9d for gold on this Market in case of undesirable competition: that would be a great help to us. There has of course always been a legal requirement that we should pay that price and legally we are free to pay more. But I have only ascertained within the last few days tgat 20 or 30 years ago, when there were heavy demands upon this Bank for sovereigns, it was the custom occasionally to pay above 77s/9d for bars. Of late, on the other hand (with no such demand for sovereigns as formerly) it has not been thought we would be wise to pay over the statutory price and the result of not having done so has doubtless tended to supply gold for the Central Banks of Europe. Before, however, I can speak definitely, I must wait to get the blessing of Addis and several others, who have strong views on gold purchases and prices. "

REICHSBANK - GERMANY

Confidential Cables

July 28 Strong to Schacht

ONE Conditions now seem to justify reducing to 3½ within the next fortnight and we expect some interior reserve banks to do so earlier.

TWO Please advise me fully of your prospects and whether further advance by you is still probable if we reduce.

THREE Outlook is for further easing of all New York rates.

FOUR Am advising Norman.

July 29 Schacht to Federal Reserve Bank, New York.

Many thanks for information. Situation here still tight hope to maintain present rate especially if your measure comes soon. Sent copy to Norman.

July 30 Harrison to Schacht

Our #2 paragraph #1 Kansas City reduced to 3½ last Thursday.

(f)

SAMPLES OF CORRESPONDENCE
W/ OTHER FR BANKS
RELATIVE TO FOREIGN CREDITS

C O P Y

FEDERAL RESERVE BOARD

WASHINGTON

January 27, 1915,

My dear Governor Strong:

I have your letter of January twenty-sixth inclosing clipping from the Annalist and copies of telegrams concerning changes in discount rates sent to you from time to time by our Secretary's office with the Board's approval.

I was sorry to have the Governors raise this question of interpretation of the law and thought that the Board had made its point of view entirely clear. Inasmuch, however, as you revert to this matter, I think it necessary to state that since the conference with the Governors the Board has fully discussed the question raised by you on their behalf and I repeat to you what was stated at the meeting, and in doing so am voicing the opinion of all the members of the Board.

The rights and duties of the Board are fully expressed in the law. It is our function to review and determine the rates. We may review and determine the rates of the Federal Reserve Banks at any time, just as much as it is incumbent upon us, when we think it our duty to do so, to require one Federal Reserve Bank to rediscount for another. To concede that the Board should have the right only to review rates when Federal Reserve Banks shall indicate their willingness to make a change, would not only be abdicating a power, but would be neglecting a duty which has clearly been imposed upon us. There cannot be any doubt that it is our function to use our influence in regulating rates to such an extent as it may be necessary to bring the various Federal Reserve Banks into harmonious relation and cooperation with each other, and to exercise such influence or power in such a way as may be indicated by the requirements of any district, or the entire country, and by its relationship to the world markets. The law clearly contemplated a central authority as a means of coordinating the twelve banks under a comprehensive policy, and the Board has determined to act upon these lines.

As you stated, you and I certainly are not very far apart in this matter. We all have only one thing in mind, and that is to achieve the best possible results, and I am convinced that when once the system will be well under way and when normal times will be re-established,the rates will originate in their natural way in the districts and that normally the Board's function will rather be to approve than to indicate rates.

Under no circumstances, however, can the Board consider for a moment failing to insist on its legal right to suggest changes in rates or to review and determine them whenever this should be required, for the best of all.

The question is of such importance that I thought that I should express myself fully and clearly upon the subject.

Very truly yours,

(signed) Paul M. Warburg

Benjamin Strong, Jr., Esq.,
Governor, Federal Reserve Bank,
New York.

C O P Y

To all F R B

FEDERAL RESERVE BOARD

WASHINGTON

December 6, 1917.

Dear Sir:

Inclosed herewith is a table showing the discount rates which have been approved by the Federal Reserve Board as of December 4th. This table shows the changes which were made by all the Federal Reserve Banks at the suggestion of the Board, except in the case of the Federal Reserve Bank of New York, which, because of conditions of a local character, has asked that action be deferred until December 15th.

The table will show greater uniformity in the rates established by the eleven banks which have acted than has existed heretofore. It has been the desire of the Board to simplify the rate schedule and the means of acting upon changes in rates. There are only two schedules for fifteen day paper, one for commercial paper and collateral notes secured by commercial paper, (including commodity paper and trade acceptances) and the other for collateral notes and customers' paper secured by Government securities. Heretofore there were four rates, as some banks charged a different rate for a note secured by commercial paper than for fifteen day commercial paper discounted, and some had a rate one-half per cent higher for member banks' customers' notes secured by Government securities than for a collateral note secured in the same way. Some banks had a special quotation for the fifteen day trade acceptances.

In telegrams which were exchanged between the Board and the banks some confusion has arisen because of difficulty in describing the character or maturity of the paper to which the rate referred. In order to avoid this in the future there has been inserted in the table a <u>code word at the head of each classification of paper, and hereafter in telegraphic correspondence regarding rates these code words will be used</u>. An additional code word has been inserted for bankers' acceptances, and two additional code words appear for commodity paper having from 16 to 60 days and from 61 to 90 days to run, for use by such banks as still maintain a quotation for this kind of paper, although for the time being the rates are the same as on ordinary commercial paper. The fifteen day rate for commodity paper shall remain merged with the fifteen day rate for commercial paper, even though a special rate for longer time commodity paper be reestablished later on.

It should be understood that fifteen day trade acceptances will be taken under whichever classification may be the lower. To illustrate, one of the banks has a trade acceptance rate of $3\frac{1}{2}\%$ for 1 to 60 days and a fifteen day commercial paper rate of 4%. Fifteen day trade acceptances will according be taken by that bank at $3\frac{1}{2}\%$. At another bank the rate is $3\frac{1}{2}\%$ for trade acceptances from 1 to 60 days and 3% for fifteen day commercial paper. In that case the trade acceptance would be taken at the commercial paper rate of 3%. The Board is of the opinion that when commercial paper or trade acceptances have run down to fifteen days, the difference in classification is not of sufficient impottance to warrant a special quotation.

Very truly yours,

Governor.

To all F R B

COPY

FEDERAL RESERVE BOARD

WASHINGTON

X-1307

December 14, 1918

SUBJECT: Rates of Discount.

Dear Sir:

You have been reporting to the Board weekly, on form No. X-877, rates of discount prevailing in your district and your recommendations as to what changes, if any, should be made. As you know, the Board requested that in order to have all reports considered at the Board meeting on Thursday, your report be in its hands each Wednesday, and carry your recommendations of rates for the succeeding week.

The Board has decided to discontinue the use of these mail reports, and requests that recommendations of changes be sent in by telegraph on each Wednesday. If it is desired to continue in effect prevailing rates, a telegram to that effect should be sent, so that the rate situation in your district may be before the Board constantly. In telegraphing changes recommended, kindly identify the various classes by the code words shown in form X-877, as follows:

	D I S C O U N T S						Trade Acceptances		Open Market Purchases.
CODE WORDS:	DAIS	DEAN	DINE	DOOR	DUAL	DRUM	DALE	DYRE	DOVE
					Secured by US certificates of indebtedness or Liberty Loan bonds				
Maturities in days	Within 15 days including member banks' collateral notes	16 to 60 days inclusive	61 to 90 days inclusive	Agricultural and live stock paper over 90 days	Within 15 days including member banks' collateral notes	16 to 90 days inclusive	1 to 60 days inclusive	61 to 90 inclusive	All maturities

Kindly acknowledge receipt.

Respectfully,

W.P.G. Harding

Governor

The Chairman,
Federal Reserve Bank,
New York, N. Y.

1

[T]o be forwarded to reach the
[F]ederal Reserve Board not later
than Thursday a.m. each week.

Date
New York, N. Y., December 11, 1918
[redacted]

Federal Reserve Board,
Washington, D. C.

Sirs:

I have the honor to forward the recommendation that no change be made in the existing discount rates for the vote of our directors, for the week ending Thursday, December 19, 1918.

(signed) R. M. Gidney
Asst. Federal Reserve Agent and
Chairman of the Board

I have the honor to request that the following rates be approved by the Federal Reserve Board for the Federal Reserve Bank of ______________________

to become effective Friday morning ______________ 191____

DISCOUNTS

CODE WORDS	DAIS	DEAN	DINE	DOOR	DUAL	DRUM	DALE	DYRE	OPEN MARKET PURCHASES
					Secured by U.S. certificates of indebtedness or Liberty Loan bonds				
Maturities in days	Within 15 days including member banks' collateral notes	16 to 60 days inclusive	61 to 90 days inclusive	Agricultural and live stock paper over 90 days	Within 15 days including member banks' collateral notes	16 to 90 days inclusive	1 to 60 days inclusive	61 to 90 days inclusive	

and so forth

O P Y

February 2, 1920.

Dear Governor Harding:

At the last meeting of our directors the proceedings in regard to the establishment of the rates of discount which were announced by this bank on January 22 were reviewed and considered, particularly with respect to the new minimum rate of 5 1/4% for the purchase of acceptances in the open market, which was fixed by the Board not only without recommendation from or consultation with our directors or officers, but as far as our officers can remember we had had no previous intimation from the Board that it felt our buying rate was too low.

The discount market which centers in New York City is a delicate affair, the resultant of adverse interests and made up of many elements, including national and state banks, private bankers, branches of foreign banks, discount houses and bill dealers. Stability is one of its essentials and, while it must necessarily fluctuate with the demand for money, yet it is important that such fluctuations should be reasonably gradual. *************
****

Our directors, accordingly, ask me to request the Board to reduce the minimum buying rate to 5% in order that there may be an element of flexibility available should it be considered advisable, from time to time, to buy very short prime import bills at somewhat less than 5 1/4%.

In sending the Board this request our directors have asked me to express to you their unanimous feeling that whatever may be the legal powers of the board in respect of fixing rates, it is desirable, if the interest and services of responsible directors are to be retained, that there should be a continuance of the practice heretofore followed of arriving at discount rates by cooperation between the bank and the Board which seems to them to be the procedure indicated by the wording as well as the spirit of the law.

Very truly yours,

Pierre Jay
Chairman.

Hon. W.P.G.Harding,
Governor, Federal Reserve Board,
Washington, D.C.

C O P Y

FEDERAL RESERVE BOARD

WASHINGTON

March 4, 1920

Subject: Recommendations covering changes in discount rates.

Dear Sir:

Since the Board no longer considers recommendations for changes in discount rates at Federal Reserve Banks upon a stated day each week, and is at all times prepared to consider such recommendations in its regular meetings, it is requested that the practice be discontinued of sending to the Board each Wednesday a code telegram submitting your recommendations regarding discount rates in your district.

The instructions regarding reports to the Board each Wednesday with respect to discount rates, contained in the Board's letters of December 14, 1918, and August 7, 1919, (X-1307, "Rates of Discount", and X-1645, "Additional Code Word for use in Discount Rate Telegrams") are accordingly revoked, and hereafter, the Federal Reserve Banks will advise the Board only when submitting recommendations for changes in the prevailing discount rates for the review and determination of the Board. When recommendations are forwarded by wire, the code suggested in the Board's letter of December 14, 1918 (X-1307) should be used.

Very truly yours,

W. T. Chapman

Secretary.

Mr. Pierre Jay,
Chairman, Federal Reserve Bank,
New York, N. Y.

RESERVE AGENT AT N.Y.
ED JAN 6 26
FERRED FOR ATTENTION TO
MR. Jay
THIS COPY FOR INFORMATION OF
MR. STRONG
" CASE
" SAILOR
" KENZEL
" HARRISON
" JAY
" Sidney
"

FEDERAL RESERVE BOARD

WASHINGTON

ADDRESS OFFICIAL CORRESPONDENCE TO
THE FEDERAL RESERVE BOARD

Acknowledged by number.

dup

X-4493

January 5, 1926.

SUBJECT: Procedure at Reserve Banks on Rates.

Dear Sir:

In order to give greater uniformity to the procedure in the matter of fixing discount and open-market rates and to provide for a consideration of these questions at each meeting of the Boards of Directors of the Federal Reserve Banks, the Board requests that each Federal Reserve Agent, in his capacity as Chairman, present to his Board of Directors a complete schedule of the rates prevailing at the bank for their consideration and action.

The schedule of rates should include the following:

1. Discount rate.
2. Minimum buying rates by maturities for bankers' acceptances.
3. Rates at which bankers' acceptances may be purchased, with agreement to resell (so-called repurchase agreements).
4. Rates at which Government securities may be purchased with agreement to resell.

Following each meeting of the Board of Directors the Board desires to be advised by telegraph of the action taken by the Directors, either in approving the existing schedule of rates, or in recommending change in any one of the rates.

A. J. L.
RECEIVED
JAN 6 1926
ATTENDED TO
Noted

Very truly yours,

READ
JAN 6 - 1926
R. M. G.

D. R. Crissinger,
Governor.

TO ALL FEDERAL RESERVE AGENTS.

File Copy. L.B.

Sample of letter sent after each directors meeting

August

September 1, 1927.

S i r s :

At the meeting of our directors held today the following schedule of existing rates was presented and no changes were made:

Discount rate - 3 1/2%.

Buying and repurchase agreement rates:

Bankers acceptances -

Minimums established by this bank:
1 to 60 days - 3%; 61 to 90 days - 3 1/4%;
4 months - 3 3/8%; 5 and 6 months - 3 3/4%;
Repurchase - 3%.

Currently effective:
1 to 45 days - 3%; 46 to 90 days - 3 1/4%;
4 months - 3 3/8%; 5 and 6 months - 3 3/4%;
Repurchase - 3 1/4%.

Trade Bills:
Minimum established by this bank - 3 1/2%;
Currently effective - 3 1/2%.

Governments:
Repurchase - 3 1/2%.

Respectfully,

J. E. CRANE,
Assistant Secretary.

Federal Reserve Board,
Washington, D. C.

IHB

Copy of this letter sent to all Governors.

Dup.

A

STRICTLY CONFIDENTIAL October 11, 1926.

Dear Governor Harding:

During the past few weeks negotiations have taken place in London between the Belgian Government and its bankers on the one hand and the National Bank of Belgium and certain banks of issue on the other hand, looking toward the establishment of loans and credits for the purpose of stabilizing the Belgian currency. Mr. Jay, who happened to be abroad at the time, was present at the meeting between the new Governor of the National Bank of Belgium, Mr. Franck, and the representatives of other central banks, and on October 3, cabled to us that the National Bank of Belgium had asked us to grant them a credit.

It was proposed that we should agree for a period of one year to purchase 90-day commercial bills drawn either in Belgian francs or other stable currency with the following understandings:

(a) That the bills when discounted would have a maturity of at least 20 days.

(b) That they would bear two names besides that of the National Bank of Belgium.

(c) That the National Bank of Belgium would agree to export gold if necessary to repay any drawings under the credit and that the Government would undertake to place no obstacles in the way of such exports.

(d) That the rate of discount would be one per cent above our discount rate, with a minimum of five per cent.

(e) That the National Bank of Belgium would defray any stamp duty payable on bills bought by us.

(f) That any amounts needed by the National Bank of Belgium under their various credits with the several banks of issue would be drawn and repaid ratably and pari passu and

(g) That the commission for our undertaking for a period of one year to purchase bills would be one half per cent per annum.

The proposal is that several central banks, which have been requested for a credit, including the Bank of England, the Netherlands Bank, the Reichsbank, the Swiss National Bank, the Hungarian National Bank and the Federal Reserve Bank, should agree to purchase or make advances upon commercial bills in amounts equal in the aggregate to five million pounds sterling or its equivalent. While neither the aggregate amount nor our amount is as yet definitely determined, it is contemplated that we should agree to purchase somewhere between five and ten million dollars.

It is understood, however, that none of the banks of issue will give any credit except as a part of a program which will comprehend an arrangement (now in process of negotiation) between the Belgian Government and its bankers in Amsterdam, Basel, London, New York, and elsewhere, for the issue of a loan or credit for an aggregate amount of not less than the equivalent of, say, fifteen million pounds, to be issued within thirty days, and the entire amount to be placed at the disposal of the National Bank of Belgium forthwith to be devoted by them to immediate de jure stabilization of the Belgian currency.

Our directors, with the approval of the Federal Reserve Board, have authorized Mr. Jay to advise the National Bank of Belgium that we will agree to purchase bills on the proposed terms and conditions set forth above, with the understanding that the legal authority of the National Bank of Belgium to purchase and guarantee bills will be satisfactorily determined. The Federal Reserve Board, however, in granting its approval, suggested a review of the condition relating to the charge of a commission. Our directors therefore intend to reconsider this question on Thursday.

While none of the terms and conditions have been finally agreed upon with the National Bank of Belgium, nevertheless, it is likely that they will be concluded within a short time, and this letter is merely to advise you of the progress of the negotiations so that you might discuss the matter very confidentially with your directors. We shall of course be glad to send you any further information that you may desire in connection with this proposed transaction and shall advise you definitely towards the end of this week regarding the proposal to charge a commission for the credit. We would then very much appreciate your prompt advice whether you care to participate with us in the event that the credit is finally arranged and made effective as outlined in this letter. I shall of course advise you if and when that is done.

We have not as yet made any statement to the press and if we later decide to do so we shall of course telegraph you its form so that you may be kept fully advised. In the circumstances I hope you will impress upon your directors the need for caution regarding the details and terms of this letter, which are most confidential and should not be made public.

Very truly yours,

GEORGE L. HARRISON,
Deputy Governor.

KMU

CONFIDENTIAL October 21, 1926.

Dear Governor McDougal:

I have just finished talking to you on the telephone and as you have requested me to give you in writing some of the matters which we discussed, so that it might go to you by to-night's air mail, in order to save time I am taking the liberty of enclosing a copy of a letter which I have to-day dispatched to Mr. Curtiss in Boston, who asked me several questions on the telephone regarding the background of this particular credit. Some of the matters referred to in this letter cover questions which you also have placed before me.

A copy of the agreement which I shall forward to you later to-day will cover some of the other questions, but as that may not reach you in time for your meeting, I am glad to tell you in reply to your first question, that the rate of exchange is guaranteed. In other words, bills bought by us, in whatever currency they are payable, bear two names plus the guaranty of the National Bank of Belgium that they will be repaid in dollars at the same rate of exchange as that at which they were purchased. Furthermore, we have take the additional precaution of getting assurances from the Belgian Government that it will interpose no obstacle in the way of the export of gold if that becomes necessary in order that the National Bank of Belgium may fulfill its guaranty to us.

You ask in your second question what would be the gold value of the proposed stabilized currency. That is a matter, of course, which is entirely within the decision of the Belgian Government, and while I presume that they, for obvious reasons, will make no statement to any one as to what that figure will be in advance of their proclamation, I understand that the figure which has been discussed from time to time is a ratio of about seven to one.

The fifth question which you ask relates to the effect of the French situation upon the proposed stabilization of the Belgian franc. That is a matter which we know has been discussed very carefully and intimately in connection with the proposed Belgian plan, and while, of course, the French price level, as any other external price level, will necessarily have some effect upon the exchange of goods between France and Belgium and a consequent effect upon the Belgian exchange, nevertheless it is believed that the present program is so conservatively worked out that Belgium will be in a position to withstand any adverse influences that might result from any possible change in the situation in France.

With the internal and external floating debts of the Belgian Government virtually eliminated or provided for, with what I understand to be a balanced budget, and with what we believe to be a capable and courageous management in the National Bank of Belgium, there is every reason to hope that the present program will be successful, although every one must realize that it is an important step that will require firm and intelligent management after being made effective. Governor Franck, the new Governor of the National Bank of Belgium, is, from all reports, the best man available in Belgium for the position. That in itself is, we believe, an important consideration. In any event, as I mentioned in my letter to Mr. Curtiss, we have felt that it is wise and proper for us to agree with the National Bank of Belgium to purchase bills under the terms which we have outlined as a part of the comprehensive program which, in our best judgment, we hope and believe will be successful.

If there is any further information that you may want or that I can give you, I know that you will be good enough to let me know. In the meantime, I hope you will please excuse this very hurried letter which I am dictating just before going into our directors meeting.

With kind personal regards, I am,

Very truly yours,

GEORGE L. HARRISON,
Deputy Governor.

Mr. J. B. McDougal,
Governor, Federal Reserve Bank,
Chicago, Ill.

GLH.MM
Enc.

CONFIDENTIAL October 21, 1926.

Dear Governor McDougal:

I have just finished talking to you on the telephone and as you have requested me to give you in writing some of the matters which we discussed, so that it might go to you by to-night's air mail, in order to save time I am taking the liberty of enclosing a copy of a letter which I have to-day dispatched to Mr. Curtiss in Boston, who asked me several questions on the telephone regarding the background of this particular credit. Some of the matters referred to in this letter cover questions which you also have placed before me.

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You ask in your second question what would be the gold value of the proposed stabilized currency. That is a matter, of course, which is entirely within the decision of the Belgian Government, and while I presume that they, for obvious reasons, will make no statement to any one as to what that figure will be in advance of their proclamation, I understand that the figure which has been discussed from time to time is a ratio of about seven to one.

The fifth question which you ask relates to the effect of the French situation upon the proposed stabilization of the Belgian franc. That is a matter which, we know, has been discussed very carefully and intimately in connection with the proposed Belgian plan, and while, of course, the French price level, as any other external price level, will necessarily have some effect upon the exchange of goods between France and Belgium and a consequent effect upon the Belgian exchange, nevertheless it is believed that the present program is so conservatively worked out that Belgium will be in a position to withstand any adverse influences that might result from any possible change in the situation in France.

With the internal and external floating debts of the Belgian Government virtually eliminated or provided for, with what I understand to be a balanced budget, and with what we believe to be a capable and courageous management in the National Bank of Belgium, there is every reason to hope that the present program will be successful, although every one must realize that it is an important step that will require firm and intelligent management after being made effective. Governor Franck, the new Governor of the National Bank of Belgium, is, from all reports, the best man available in Belgium for the position. That in itself is, we believe, an important consideration. In any event, as I mentioned in my letter to Mr. Curtiss, we have felt that it is wise and proper for us to agree with the National Bank of Belgium to purchase bills under the terms which we have outlined as a part of the comprehensive program which, in our best judgment, we hope and believe will be successful.

If there is any further information that you may want or that I can give you, I know that you will be good enough to let me know. In the meantime, I hope you will please excuse this very hurried letter which I am dictating just before going into our directors meeting.

With kind personal regards, I am,

Very truly yours,

GEORGE L. HARRISON,
Deputy Governor.

Mr. J. B. McDougal,
Governor, Federal Reserve Bank,
Chicago, Ill.

GLH.MM
Enc.

CONFIDENTIAL October 21, 1926.

Dear Mr. Curtiss:

In reference to our telephone conversation of yesterday afternoon concerning our proposed arrangement with the National Bank of Belgium, I am glad to send you my rather hurried comments regarding the matters which you asked me to write you.

First of all you wanted to know whether Secretary Mellon is familiar with the negotiations which have been in progress and whether he approves of our proposal to give a credit to the National Bank of Belgium along the lines outlined in my letter to you of October 11. It so happens that Secretary Mellon was in London when Governor Strong was there in September and he became thoroughly familiar not only with the proposal of the Belgian Government to effect a de jure stabilization of its currency, but also with much of the background out of which the proposal for the present credit to the National Bank of Belgium arose. Since Mr. Mellon returned home, we have kept him fully advised of each stage in the negotiations, and I think I can assure you of his full approval of the action of our directors in agreeing to purchase bills from the National Bank of Belgium under the terms and conditions set forth in my earlier letter to you. Incidentally, Mr. Mellon was present and took part in the discussions at the meetings of the Federal Reserve Board when the action of our directors in this matter was approved by the Board, and he has since expressed to me his own personal interest in and approval of our proposed participation in the program.

Another matter which you suggested for comment is one which involves the propriety of our participating in arrangements of this character. I think there can be little question of our legal authority to purchase commercial bills at home or abroad nor of our right to make an agreement to exercise that right, for a period of time. From a legal aspect this agreement is similar to the temporary one which, with the Federal Reserve Board's approval, we made with the National Bank of Belgium last winter. In that agreement all Federal reserve banks participated. It seems to us, therefore, that the only question of propriety which might be asked is whether our purpose in entering such an agreement is in all the circumstances a sound one.

It has been the belief of the officers and directors of this bank, since efforts were first made abroad to reestablish the gold standard, that we should cooperate within the limits of our powers in aiding banks of issue, who are our correspondents and agents abroad, to take their part in a program of stabilization having reasonable prospects of success. Entirely apart from any moral obligation we may have to aid in the reestablishment of the gold standard in those countries whose exchanges have been seriously deranged because of the war or post-war influences, we believe that from a wholly selfish standpoint one of the most effective ways in which the Federal Reserve System can aid our own agriculture, commerce and industry is by rendering every proper assistance in the stabilization of the currencies in those countries to which we seek to export our surplus products. Owing to the mal-adjustment of international exchanges during the past ten years we have accumulated a large percentage of the world's monetary gold. We believe that it would be most short-sighted were we to adopt any policy which would now discourage the reestablishment of the gold standard in other countries, which would delay the return to the free shipments of gold between nations in settlement of trade balances, or which would make our own large stock of gold any less useful to all or less valuable to us.

But as you say, it has been suggested that these purposes might be accomplished through the private banks and bankers rather than through the Federal reserve banks. That of course is a question which might be susceptible to different opinions. It should be remembered, however, that the problem of monetary stability is peculiarly a matter within the province of the banks of issue, that no successful program of stabilization can be accomplished without the aid or cooperation of the bank which issues the currency to be stabilized, and that, as we view it, it is wholly natural and proper that the bank of issue should turn to other banks of issue which are its correspondents for assistance in their peculiar problem. On the other hand, we believe that it is also natural and proper that the foreign government or its finance minister should seek aid in its part of a stabilization program, not from the banks of issue abroad, but from its own bankers in those foreign countries where they may be seeking loans. Sometimes the line of demarcation between these two functions is difficult of determination but the principle involved seems clear and in the present case, as in the case of England, the Belgian Government has sought its loans from its own bankers and the National Bank of Belgium has turned for the aid which it needs to other banks of issue which are its correspondents. It is in response to their request in these circumstances that we have agreed to the present credit.

While these two functions of the government and the bank of issue are separate and distinct in themselves, nevertheless, they are inter-dependent in that each is a necessary part of the complete program. In considering the present proposal our directors would clearly not have approved of our entering an arrangement with the National Bank of Belgium for the purpose of assisting in the stabilizing of its currency had we not been assured that the Belgian Government on its part has been making arrangements with its bankers for loans which would enable it successfully to carry out its part of the program. By the same token I think it is fair to say that the bankers of the Belgian Government probably would have been loath to proceed with their negotiations had they not been satisfied as to the management and policies of the National Bank of Belgium which they understand is the institution that will have to carry through the program once adopted. The fact that other central banks of issue which are the correspondents of the National Bank of Belgium are satisfied in all the circumstances to extend it credits is of itself a strong influence in satisfying the bankers on this point and encouraging them to proceed with their part of the program. In this connection it is generally realized that confidence in a program of stabilization is a quite vital factor in its success. That foreign banks of issue stand ready to give credits in one form or another to the bank which must be responsible for the management of the program is a most important element in creating confidence.

Still another matter to which you referred is the fact that the proposed credit contemplates our buying not only bills payable in Belgian francs but bills payable in other stable currencies. The reason for this latitude is a practical one. The National Bank of Belgium holds in its portfolio a large percentage of bills payable in foreign currencies which they need to have available for sale along with their own domestic bills. In either event we have the guaranty of the National Bank of Belgium to repay us in gold at the same rate of exchange as that at which we purchased the bills. We will also have the assurance of the Belgian Government that they will interpose no objection to the National Bank of Belgium's exporting gold if it is necessary for them to do so.

I think this covers the matters concerning which you asked me specifically for comment. There is one other matter which was left open in the letter I wrote you on October 11. That concerns the commission charged for granting the credit. As I had indicated to you, the Federal Reserve Board, in approving of our negotiating a credit with the National Bank of Belgium under the conditions I then outlined, suggested a review of the charge of a commission, expressing the belief "that a commission is not called for in connection with the purchase of prime bills by the Federal Reserve System indorsed by central banks." As suggested by the Board, our directors reviewed this matter most carefully and seriously last week. It was their best judgment after reviewing all the arguments pro and con that it is quite proper and right that, entirely apart from the discount received on bills bought, we should charge for the service rendered in committing ourselves for a specified period of time to purchase a given amount of bills. They therefore voted to charge a commission in this case but with the understanding that in order not to be charging the National Bank of Belgium at the same time that we are not charging the Bank of England, we will rebate such part of our commission as covers the period that the Bank of England credit still has to run.

For your confidential information we have now authorized Mr. Jay, who is abroad, to sign the agreement with the National Bank of Belgium to purchase $10,000,000 of commercial bills under the terms and conditions outlined to you in my earlier letter. While we are committed, therefore, in any event, we would be glad if your board of directors, after careful consideration of the whole matter, should decide to participate with us in this agreement as in other agreements in which all Federal reserve banks now participate. If there is any further question they might wish to ask, I hope you will please be good enough to let us know. But if there is no further information which we can furnish you, we should like to have you advise us as soon as may be convenient whether or not you care to participate.in this case.

I am sure that you and your directors will appreciate the confidential character of all the terms and conditions regarding this credit, which have been sent to you in confidence and not for publication. If we are to make a statement when the whole program of stabilization is finally completed, I shall of course advise you by telegraph so that you may be familiar with the facts given to the press.

With kind personal regards, I am,

Faithfully yours,

GEORGE L. HARRISON,
Deputy Governor.

Frederic H. Curtiss, Esq.
Chairman, Federal Reserve Bank of Boston,
Boston, Mass.

GLH/MM

AN IDENTICAL LETTER WAS SENT TO MR. FREDERIC H. CURTISS OF BOSTON.

STRICTLY CONFIDENTIAL   October 22, 1926.

Dear Governor McDougal:

In order to supplement my letter of yesterday, I am glad to enclose herewith a copy of the Agreement defining in detail the terms and conditions under which we have obligated ourselves to purchase prime commercial bills from the National Bank of Belgium.

I know that you and your directors will realize the confidential character of the terms and conditions of the credit covered in the enclosed agreement as well as in my earlier letter. We have as yet made no public statement and although we shall probably do so when the program of the Belgian Government is finally completed and announced, probably next week, we shall of course advise you by telegraph so that you may be entirely familiar with the facts given to the press.

This letter and its enclosure is sent to you to supplement my letters of October 11 and 21, and my telegram of last night in which we told you of the completion of the agreement and asked for your advice whether you might care to participate with us on the usual basis.

With many thanks for your most helpful cooperation, I am,

Very truly yours,

GEORGE L. HARRISON,
Deputy Governor.

Mr. J. B. McDougal,
Governor, Federal Reserve Bank,
Chicago, Ill.

GLH.MM
Enc.

TO ALL GOVERNORS EXCEPT BOSTON AND CHICAGO

dup

STRICTLY
CONFIDENTIAL

October 22, 1926.

Dear Governor

In confirmation of my telegram of yesterday, I am glad to advise you that we have agreed with the National Bank of Belgium to purchase $10,000,000 of prime commercial bills under the terms and conditions set forth in detail in the enclosed Agreement, which as you will see is in substantial conformity with the terms briefly outlined in my letter of October 11.

While each of the provisions in the agreement is, we think, self-explanatory, there is one clause about which some comment is needed, that is, clause eleven which provides for a commission of one-half of one per cent. of the amount of the credit.

As I indicated in my letter of October 11, the Federal Reserve Board in approving of our entering into an agreement with the National Bank of Belgium under the terms and conditions then outlined, suggested a review of the clause relating to a commission, expressing the belief "that a commission is not called for in connection with the purchase of prime bills by the Federal Reserve System indorsed by central banks." As suggested by the Board, our directors reconsidered this matter most carefully and seriously last week. It was their best judgment, after reviewing all the arguments pro and con, that it is quite proper and right that, entirely apart from the discount received on bills bought, we should charge for the service rendered in committing ourselves for a specified period of time to purchase a given amount of bills. They, therefofe, voted to charge a commission in this case, but in order not to be charging the National Bank of Belgium a commission at the same time that we are not charging the Bank of England, it is our intention to make a pro rata rebate of such part of the commission as covers the period of the unexpired part of the Bank of England credit, on which, as you know, no commission is charged.

I am explaining this in some detail because there is no reference in the agreement itself to our purpose in regard to a refund. We hope, however, that you will agree with us in the circumstances that this partial rebate should be made.

For your information I am taking the liberty of enclosing a copy of a confidential letter which I wrote yesterday to Mr. Curtiss of the Federal Reserve Bank of Boston in reply to some questions he raised concerning some of the aspects of the credit. It may be that it will be of interest to you or to some of your directors. But if there are any further questions which you might have in mind I hope that you will please be good enough to let us know.

I know that you and your directors will realize the confidential character of the terms and conditions of the credit covered in the enclosed agreement as well as in my earlier letter. We have as yet made no public statement and although we shall probably do so when the program of the Belgian Government is finally completed and announced, probably next week, we shall of course advise you by telegraph so that you may be entirely familiar with the facts given to the press.

This letter and its enclosures are all sent to you to supplement my earlier letter of October 11 and my telegram of last night, in which we advised you of the completion of the agreement and asked for your advice whether you might care to participate with us upon the usual basis.

With many thanks for your most helpful cooperation, I am,

Very truly yours,

GEORGE L. HARRISON,
Deputy Governor.

Enc.
GLH/KMC

TO ALL GOVERNORS EXCEPT BOSTON AND CHICAGO

dup.

STRICTLY
CONFIDENTIAL

October 22, 1928.

Dear Governor

In confirmation of my telegram of yesterday, I am glad to advise you that we have agreed with the National Bank of Belgium to purchase $10,000,000 of prime commercial bills under the terms and conditions set forth in detail in the enclosed Agreement, which as you will see is in substantial conformity with the terms briefly outlined in my letter of October 11.

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With many thanks for your most helpful cooperation, I am,

Very truly yours,

GEORGE L. HARRISON,
Deputy Governor.

Enc.

GLH/KMC

A copy of this letter, with enclosure, was sent to the Governor of each F.R. Bank.

CONFIDENTIAL

October 25, 1926.

Dear Mr. Curtiss:

I am glad to advise you that the credit arrangement with the National Bank of Belgium, a copy of which I sent to you in my letter of October 23, was finally delivered and made effective as of to-day, so that it will run for a period of one year from October 25, 1926.

I want also to let you know that the Bank of France has participated in the agreement for the amount £1,000,000, and appropriate reference to that fact should be made in the agreement.

For your further information, I am enclosing a copy of the Royal Decree of Monetary Stabilization which was signed by the King yesterday and which went into effect upon its publication in Brussels to-day.

Very truly yours,

GEORGE L. HARRISON,
Deputy Governor.

Frederic H. Curtiss, Esq.,
Chairman, Federal Reserve Bank of Boston,
Boston, Mass.

Enc.

GLH/KMC

TO ALL GOVERNORS

B

STRICTLY CONFIDENTIAL June 22, 1927.

My dear Governor Harding:

You may remember that at the recent Conference of Governors we referred in some detail to the efforts then being made by the Government of Poland to devise a program of monetary stabilization.

We reported that Dr. Mlynarski, Vice Chairman of the Bank of Poland, had come to this country early in February first to represent his Government in discussing a program of stabilization and a stabilization loan with the bankers of his Government and second to confer with the Federal reserve bank concerning the monetary aspects of the program. We also referred to the views exchanged with Governor Norman, Dr. Schacht and Governor Moreau concerning a possible credit to the Bank of Poland in the event that the banks of issue should be asked for a credit as Dr. Mlynarski had indicated they would be.

In order to keep you fully informed we want now to let you know that on June 2, 1927, we received a telegram from the Bank of Poland advising us that its Government had approved of a program of stabilization, a copy of which was forwarded to us through the New York bankers of the Polish Government, and that the Bank of Poland wanted to know whether we would be prepared now to discuss terms and conditions of a credit. On June 6, 1927, the Federal Reserve Board approved of the action of our directors in authorizing us to make an arrangement with the Bank of Poland for the purchase of up to $10,000,000 of prime commercial bills. For your information I am enclosing a copy of our letter to the Board as well as their letter of approval.

Since that time we have been negotiating terms and conditions for an arrangement with the Bank of Poland closely following the lines of the arrangement with the National Bank of Belgium. In brief, the arrangement as now proposed will comprise the equivalent of a $20,000,000 credit to the Bank of Poland in which about fifteen banks of issue will participate. The arrangement will be for a period of one year from the date of final legal promulgation of the program of stabilization by the Polish Government. The rate charged will be six per cent except that in any case where the discount rate of the participating bank of issue exceeds six per cent, then the rate charged to the Bank of Poland by that bank shall be the same as its discount rate. A commission of one-half of one per cent will be charged by each participant on its share in the arrangement as was done in the case of the Belgian credit. At the moment it seems likely that the Federal reserve bank will agree to purchase up to $6,000,000 of bills, that the Bank of England, the Reichsbank and the Bank of France will each take the equivalent of $3,000,000 and that approximately ten other banks of issue will take the balance of the $20,000,000 in varying amounts.

One clause in the arrangement provides that the granting of the credit will be subject to the final legal promulgation of the program by the Polish Government, which is to include a loan by the Government's bankers to the Government aggregating approximately $60,000,000, of which we understand about $25,000,000 is to be issued abroad. It so happens that at the moment the market for new issues of bonds in New York is somewhat congested. That fact, coupled with the recent unfavorable publicity regarding the murder of the Soviet Minister at Warsaw, has made the bankers decide to defer an issue of bonds for the present. As a result, while the arrangements for the credit by the banks of issue to the Bank of Poland are proceeding, nevertheless, it seems unlikely that the program, upon which that credit will depend, will be finally consummated until a more auspicious moment for the issue of a loan.

This is but a brief outline of the status of the proposed arrangement with the Bank of Poland and is intended merely to keep you informed of the progress which has been made and to let you know that it seems likely that the arrangement will be concluded in the near future when we shall of course offer you a participation on the usual basis.

In the meantime please regard this letter as most confidential and if there are any questions which you might care to ask, I hope you will be good enough to let us know.

Very truly yours,

G.L.H.
mc
GEORGE L. HARRISON,
Deputy Governor.

Mr. W. P. G. Harding,
Governor, Federal Reserve Bank,
Boston, Mass.

Encs.

GLH.KMC

To all Governors

STRICTLY CONFIDENTIAL June 29, 1927.

Dear Governor Harding:

On June 22 I wrote to you concerning the status of the negotiations for a credit to the Bank of Poland. In order to supplement that letter, I am glad to enclose herewith for your confidential information a copy of the Program of Stabilization as agreed upon by the Polish Government and their bankers, as well as a copy of the proposed bank of issue agreement with the Bank of Poland. As you will, of course, realize the Program of Stabilization has been given to us in strict secrecy pending its final legal promulgation by the Polish Government. Inasmuch, however, as the request of the Bank of Poland for a credit from the banks of issue is predicated in part on this program, you may be interested in examining it together with the draft of agreement with the Bank of Poland so that you may have it in mind in determining whether or not you care to participate with us in the bank of issue credit.

Loose in file

This arrangement with the Bank of Poland has been agreed to in principle by the various banks of issue listed in Clause 17 of the agreement and is now being forwarded to each of them for signature with the understanding, as specified in Clause 16, that if the legal promulgation of the Program of Stabilization and the issue of the loan provided for in that program are not consummated before August 20, 1927, the credit shall not become effective. While we have not yet actually signed the agreement, which is being forwarded to us from Paris where it was printed and signed by the representatives of the Bank of Poland, nevertheless we expect to do so as soon as it is received in New York. Even though the credit will not become effective until the final legal promulgation of the program by the Government and the issue of the loan by the bankers, nevertheless will you please be good enough to let us know, after you have had an opportunity to study all the documents, whether you care to participate with us in our agreement to purchase up to $5,250,000 of prime commercial bills under the terms and conditions set forth.

I understand that the bankers do not yet feel that it is time to float a long term bond issue as contemplated by the Program of Stabilization. They are, however, discussing with the Polish Government the granting of a short term credit of approximately $15,000,000 pending the issue of the bonds. This credit is entirely independent of the bank of issue credit which is to be granted to the Bank of Poland and which will become effective only on the conditions outlined in Clause 16.

Because of the status of this whole matter and the uncertainty of the date of final action by the Polish Government and its bankers, you will, I am sure, appreciate the need for regarding it and the enclosed documents in the strictest confidence. Please do not hesitate to let us know if there are any further questions you may care to consider before advising us whether you will participate on the usual terms.

Very truly yours,

G. L. H.
mc

GEORGE L. HARRISON,
Deputy Governor.

Mr. W. P. G. Harding,
Governor, Federal Reserve Bank,
Boston, Mass.

Encs.

GLH.MM

THIS LETTER SENT TO:

Governor	F. R. Bank of
Norris	Philadelphia
Fancher	Cleveland
Seay	Richmond
Wellborn	Atlanta
McDougal	Chicago
Biggs	St. Louis
Young	Minneapolis
Bailey	Kansas City
Talley	Dallas
Calkins	San Francisco

STRICTLY CONFIDENTIAL

August 10, 1927.

Dear Governor Harding:

Referring to our letter of June 29, concerning the Central Bank Credit to the Bank of Poland, and to your participation with us in this agreement, we explained that if the legal promulgation of the program of stabilization and the issuance of the loan are not consummated before August 20, 1927, the agreement with the Bank of Poland shall not become effective. When this time limit was fixed, it was contemplated that an extension might be required.

The private bankers have recently advised the Polish Government that it would be inadvisable to attempt a large public offering in this market, such as the program contemplates, before the middle of September, unless conditions should suddenly change. At the suggestion of the Bank of France and in concurrence with the Bank of England and the Reichsbank, we have agreed to the extension of this date from August 20 to November 1, 1927, which would permit of the issuance of the loan and the promulgation of the program in October, if necessary.

Very truly yours,

BENJ. STRONG,
Governor.

Mr. W. P. G. Harding,
Governor, Federal Reserve Bank of Boston,
Boston, Massachusetts.

JEC HAB

THIS LETTER SENT TO EACH GOVERNOR OF OTHER FEDERAL RESERVE BKS.

CONFIDENTIAL

August 22, 1927.

Dear Governor Harding:

We have received a request from the Austrian National Bank, Vienna, to open an account for it on our books and invest its funds in bankers acceptances.

The Austrian National Bank opened its doors on January 2, 1923 after having assumed the assets and liabilities of the Austrian Section of the Austro-Hungarian Bank and having absorbed the Central Exchange Bureau. It is an independent joint-stock company with a share capital of 30 million gold kronen (about $6,000,000) which was fully paid up in June, 1923. The bank is under the direction of a board, all the members of which are elected by the shareholders with the exception of the Chairman who is appointed by the President of the Austrian Confederation.

According to the banking law and the statutes, the operations of the Austrian National Bank must be purely commercial and the bank is expressly forbidden to grant directly or indirectly any advances to the State, the Provinces or the Communes unless they cover in gold or foreign currencies the amounts issued to them in bank notes. The Government controls somewhat more than one-quarter of the share capital.

Of the net profits less the statutory deductions to be made for a reserve fund and a pension fund, two-thirds to three-quarters, depending upon the amount of these profits, will be allocated to the State, the rest being used for dividends. According to an agreement between the Government and the bank,

part of the profits allocated to the State will be used for paying off the State debt to the bank. A copy of the bank's balance sheet as of July 31, 1927 is enclosed.

At the meeting of our board of directors on August 18, the officers were authorized to open an account on our books for the Austrian National Bank, to establish a relationship with that bank along the same general lines as our arrangements with other foreign central banks, and to appoint the said bank as our agent and correspondent in return for a similar appointment from it.

The Federal Reserve Board has approved of the foregoing action of our directors, and we are opening an account to-day for the Austrian National Bank, the initial deposit therein being $1,000,000 most of which will be invested in bills.

While it is not likely that this account will be very active for the present owing to the fact that the Austrian National Bank is restricting its investments in bills because of the tax on discount earned on bills held by a foreign corporation, nevertheless we would like to offer you an opportunity to participate in the account upon the usual basis, and would be pleased to learn whether or not you care to do so. If so, may I ask you to send us telegraphic advice in order that the participation of the account may be made as promptly as possible.

With kind regards, believe me

Very truly yours,

J. H. CASE,
Deputy Governor.

Mr. W. P. G. Harding,
Governor, Federal Reserve Bank,
Boston, Mass.

JEC:MK

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<u>CONFIDENTIAL</u> August 22, 1927.

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With kind regards, believe me

Very truly yours,

J. H. CASE,
Deputy Governor.

Mr. W. P. G. Harding,
Governor, Federal Reserve Bank,
Boston, Mass.

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With kind regards, believe me

Very truly yours,

J. H. CASE,
Deputy Governor.

Mr. W. P. G. Harding,
Governor, Federal Reserve Bank,
Boston, Mass.

JEC:MK

(G)

Extracts from Articles of assn. of Chicago Clearing House assn. and NY Clearing House assn. Relative to Interest on Deposits.

A.

ARTICLE XI

Where Interest Rates Apply

Section 3. Except as otherwise provided in Section 1 of this Article, no member of this Association, nor any non-member clearing through a member, shall pay or agree to pay directly or indirectly interest on any credit balance or on any certificate of deposit in excess of the rate fixed from time to time by the Clearing House Committee to any person or persons, corporations, associations, or co-partnerships, residing, organized, located or having its principal place of business in Continental United States, Alaska, Hawaii and the Dominion of Canada, provided, however, that any rate so fixed shall not apply to credit balances of and/or certificate of deposit issued to any person, corporation, association or co-partnership located or having its principal place of business outside of Continental United States, Alaska, Hawaii, or the Dominion of Canada, or to the Government of the United States of America or any department, territory or dependency thereof, to the District of Columbia, to any state of the United States, or any sub-division thereof, nor shall they affect interest rates now or hereafter fixed or regulated by law; provided however that any foreign branch maintained pursuant to legal authority by any member of this Association or by any non-member clearing through a member, shall be permitted to pay, on deposits received by such branch in the normal course of its business, interest at the current rates prevailing where such branch is located.

No member, nor any non-member, clearing through a member, shall however solicit, directly or indirectly, or use any branch in a foreign country for the purpose of soliciting, American Dollar deposits from persons, corporations, associations or co-partnerships residing, organized, located or having its principal place of business in Continental United States, Alaska, Hawaii or the Dominion of Canada, by offering rates of interest thereon higher than those then prescribed by the Clearing House Committee with respect to deposits in New York City unless the deposit solicited is to be made in a branch in a foreign country in which the currency is United States Dollars and such deposit will be maintained for the normal requirements of the business of the depositor in that country.

B.

CHICAGO CLEARING HOUSE ASSOCIATION

January 28, 1920.

The following resolution in regard to payment of interest on bank deposits was unanimously adopted by the members of the Chicago Clearing House Association at a meeting held this day, effective immediately.

No member of this Association and no bank or trust company clearing through any member shall agree to pay, or shall pay, directly or indirectly, on any credit balance payable on demand or within ten days, or on any certificate of deposit so payable, by its terms, issued to or for the account of any bank, trust company, or other institution conducting a banking business, or private banker or bankers, located in the United States, interest at a rate in excess of one per cent per annum when the then ninety-day discount rate for commercial paper at the Federal Reserve Bank of Chicago is two per cent or less, and an additional one-fourth of one per cent for every one-half of one per cent that such discount rate of the Federal Reserve Bank shall exceed two per cent, except that the maximum rate paid or agreed to be paid on any such credit balance or certificate of deposit shall not in any case be higher than two and one-fourth per cent per annum.

(H)

Conference of Governors 1/20-23/1915

A

C O P Y

Topic #20 - DISCOUNT RATES - was then taken up for discussion. This discussion covered not only the question of the initiation and establishment of discount rates by the Federal reserve banks for member banks, but also the proper method to be pursued in case it should be desired to establish rates of discount between the Federal reserve banks themselves. On motion duly made and seconded, it was

> VOTED that the Chairman be requested to present to the Federal Reserve Board a fair consensus which would represent the views of those in attendance at the meeting who had discussed the matter thoroughly with their respective Boards of Directors as well as at this Conference.

Mr Harrison

B

M E M O R A N D U M

To be attached to the copy of the discussion of the subject of the initiation of rate changes by the Federal Reserve Board at the Conference of Governors, ~~June~~ Jan'y 20-23, 1915.

Pursuant to the resolution adopted at the meeting above referred to, directing me to make a report at the Joint Conference of the Members of the Federal Reserve Board with the Governors of the Federal Reserve Banks, I reviewed orally and at great length the views expressed at the separate meeting of the Governors held the evening before. And the statement, which was merely a repetition of those views, ended by my advising the Board that it was the unanimous view of the Governors that in case the Board endeavored to assert its right to initiate changes in discount rates, the Banks should test the power to do so in the Courts.

A part of the discussion upon which my oral statement was based was purposely left out of the stenographic record.

Benj. Strong
Chairman, Governors Conference.

(Dictated 9.12.27)

C.

COPY

The Chairman: No. 20 is the question of discount rates and the action of the Federal Board in regard to them.

Mr. Aiken: Preliminary, Mr. Chairman, to that discussion, I would like to call the Governors' attention to the exact wording of that paragraph (d) under Section 14, which seems to me to be the essence of the whole thing.

The Chairman: Will you read the reference that you refer to into the record, Governor Aiken?

Mr. Aiken: (Reading):

"ESTABLISHED RATES OF DISCOUNT.

"91(d). To establish from time to time, subject to review and determination of the Federal Reserve Board, rates of discount to be charged by the Federal Reserve bank for each class of paper which shall be fixed with a view of accommodating commerce and business."

What I had in mind was the phrase, "establish from time to time."

The Chairman: The discussion of this matter has been undertaken at different times, informally, and I believe that all of the Governors have decided views as to what our attitude should be in this matter, which is a very important one of policy; and if someone would make a motion expressing their personal views of what action should be taken by this meeting, it would give us an opportunity to discuss it with some chance for a conclusion.

Mr. O. Wells: Mr. Chairman, I undertake to move that during our meeting tomorrow we express to the Federal Reserve Board in session the probable effect that will ensue if the practice of fixing the rate by the Board by suggestion as to what the rate should be should be followed, without the same having been initiated by the Federal Reserve banks, as seems to be clearly intended by the language of the Act, those effects being, minimizing the scope of authority and policy of not only the executive officers of the Federal Reserve Banks, but the directors as well; and that in doing so we naturally give them an opportunity to discuss with us that matter, in order that there may be some understanding between ourselves as representatives of the Federal Reserve banks and the members of the Federal Reserve Board.

The Chairman: Governor Wells has suggested that our policy should be to make an expression to the Federal Reserve Board tomorrow of the view of this conference. Personally, I am heartily in accord with that policy. It occurs to me that it would be very effectively made to the Federal Reserve Board if we were able to submit to them a resolution which would carefully, conservatively and unanimously express the sense of this meeting; that resolution having due regard to the fact that each of these Federal Reserve banks is really managed by, and the executive officers are subject to, direction of directors in our respective districts who are men of importance with local experience, and, in some cases, very positive views; and that while we may be able personally to arrange these matters in a friendly way with the Federal Reserve Board, we have got to regard the fact that we have directors at home who are entitled to consider that we represent not our own personal views, but a composite of the views of the directors of the Federal Reserve banks who have great responsibilities themselves which they want to discharge.

Mr. Wold: Mr. Chairman, the directors of the Minneapolis bank have carefully considered this paragraph in reference to rates and are unanimous in their opinion that the initiation of the rate falls upon the bank, and it was such an important matter that we do not believe we want to delegate that power to the Executive Committee and provided in their by-laws that the change of rate can only be effected by a majority of the Board of Directors. And now, to have the Federal Reserve Board initiate rates here and then make it necessary for us to telephone around to secure the consent or approval of the majority of the board, makes it very embarrassing not only to the management but to the directors themselves. They feel that it is a duty of their own.

I second Mr. Wells' motion.

Mr. Seay: I would like to say, Mr. Chairman, that I feel that there is no one particular which would deliver the management of the reserve banks more over to the Federal Board than this one of fixing the rate. It is something which takes the control of the resources out of the hands of the executives of the Federal Reserve banks. It is one of the most vital things, I think, to our own autonomy that we have to consider.

Mr. Fancher: May we have the motion read, as stated by Mr. Wells?

The Chairman: Might I be permitted the suggestion that this is such an important matter that I am going to take the liberty of asking each of those present to express his views, based upon the statement that I made, that we are not expressing our individual views only, but in this matter we are really speaking for a bank in each instance which is managed by a Board of nine directors.

With your permission I will ask each of the Governors to state his position in the matter, with the fact in mind that you are speaking in a representative capacity; and at the conclusion I will ask the stenographer to read Governor Wells' motion.

Governor McDougal?

Mr. McDougal: The matter of fixing discount rates is one that has been discussed by our board a number of times, and they have been individually and collectively opposed to the initiation of the rates coming from Washington, feeling that they were entitled under the act to indicate the rate that they thought should prevail. I feel quite sure that they would like to have the opportunity of availing themselves of that privilege without interference from the Board; knowing, of course, that they have the right to refuse if they see fit.

Mr. O. Wells: I should like to correct that, if I may: That they <u>must</u> review; not if they see fit. They must determine before our action becomes operative.

The Chairman: Governor Wells, I would not like to have that statement appear on the record as accepted by the Governors present, because I am advised by counsel that that is not the case.

Mr. O. Wells: I was only trying to use the language of the Act.

The Chairman: I will state what our understanding is in this matter of the rate. The Federal Reserve Act provides that the Federal Reserve banks shall establish rates of discount, subject to review and determination by the Federal Reserve Board. That does not mean, as we construe the language, that the rate once established by the bank does not become effective until it has been reviewed, but the minute that the Federal Reserve bank establishes that rate it can commence doing business at that rate, and that the power of the Federal Reserve Board is limited to requiring, if you please, a suspension of the operation of the rate until they review it and determine it.

My personal opinion about this matter, which I believe is shared by the directors of our bank --- certainly by Mr. Curtis, who has advised us in the matter --- is that we are really entitled to establish a rate, and within five minutes to discount paper at that rate; that our duty is certainly to report it by the promptest possible means to the Federal Reserve Board, and that their duty is undoubtedly to review it and determine the rate, finally; that the establishment of the rate is a matter that rests within the power of the directors of the Federal Reserve Bank.

As a matter of fact, this custom which is developing of suggesting a rate, I believe is fraught with danger; that it may result in each Federal Reserve bank gradually getting into the position where it must respond to a suggestion because some other bank has established a rate which influences the Federal Reserve Board to force uniformity. I do not believe that that is going to be a sound development of this system; that if any Federal Reserve bank succeeds in establishing a rate that is out of line with local conditions, or with conditions that necessitate rates in other districts, it may be their misfortune to be loaded up with discounts that they have taken at very low rates, and in order to protect themselves they may be obliged to take some losses to relieve themselves of the load. Certainly any other policy applied to the making of rates is a very unnatural banking policy, because it makes a rate regardless of what the local condition may be.

Governor McCord, may I ask you to express your views in regard to this matter?

Mr. McCord: Mr. Chairman, I think that the rate should be initiated at the reserve bank, and not at the Board. It should not be published until the Reserve bank has determined absolutely on the rate, and due regard should be given to their local conditions, regardless of those of the entire country.

The Chairman: Governor Aiken?

Mr. Aiken: Mr. Chairman, I feel that the rates should be established by the banks in each district, and that the initiative should lie in the bank and not in the Federal Reserve Board.

The Chairman: Governor Fancher?

Mr. Fancher: For our board, we have rather resented these suggestions coming from the Federal Reserve Board, mentioning the lowering of rates in some of the other districts. They feel that they were given the right under the law to establish rates, and that they were best qualified to judge conditions in the district and determine what should be the prevailing rate. That is their privilege, and should continue to be their privilege under the Act.

Mr. Kains: Mr. Chairman, the directors of our board who do not directly owe their appointments to the Government, I think are unanimous in their feeling of surprise and resentment at having suggestions made to them. However, I do not think that that applies to the Government directors. That is just my opinion. We have taken no action on the matter at all except that personally I am a believer in the autonomy of the Federal Reserve banks, and I heartily agree with your statement that we should establish these rates. We know more about them; we know more about our own local conditions than anybody else does, and we feel competent to establish these rates. We should be very glad to act. We do not desire at all to act in any way contrary to the desire of the Federal Reserve Board, but we feel that we have that right, and that we know more about things within our boundaries than they.

The Chairman: Governor Wold?

Mr. Wold: Mr. Chairman, the directors of our bank are thoroughly in accord with the statement made by Governor Strong. They feel quite strongly that the law clearly intended that the rate should be initiated by the various Federal Reserve banks, and they resented the suggestions of the Federal Reserve Board as to rates, and disapprove of the announcement of rates from Washington before they are announced at the headquarters of our bank. The announcements should be made by the banks themselves, and the rates should be initiated or the change should be initiated at that bank subject to confirmation by the Federal Reserve Board. Our opinion is that when the rate is initiated it should go into effect and remain in effect until the Board have either confirmed or refused to confirm.

The Chairman: Governor Wells, your statement is already on the record in the formal motion which was seconded by Governor Wold.

Mr. O. Wells: I should like to add, inasmuch as the expressions have taken the turn of representing the opinions of the various boards, which my motion did not include, perhaps, that we have never had a formal expression of the attitude of our board on this subject. We have it expressed without any form, but I think I reflect their expression when I say that they do regret the action of announcing a willingness to make a rate before it has been discussed by the Board of Directors of the Federal Reserve Bank of Dallas. At our initial meeting the Board were of the opinion that this was a matter of sufficient importance not to be delegated to an executive committee, but that we should follow the suggestions of the by-laws submitted at the conference in October, that the making of the rate should be vested in the Board of Directors of the bank.

I frankly confess that we have been proceeding upon that theory, and that it was essential to submit the rate, having made it, for review and determination, and that the whole operation was necessary before the rate became fixed, and we had no other thought in mind.

The Chairman: The expressions of the Governors present apparently are almost identical in terms, and the scope of our resolution or recommendation in this matter can be considerably enlarged for submission to the Federal Reserve Board over what was contained in Governor Wells' motion if he and the seconder, Governor Wold, are willing for the moment to withdraw.

Mr. O. Wells: I am quite willing to withdraw the motion, with the understanding that it will be covered in the form of a resolution of sufficient breadth to include the expressions to which we have listened around the board.

The Chairman: Gentlemen, what is your pleasure as to the method that we should employ in expressing the consensus of opinion of those present with regard to this matter of the method by which rates are made?

Mr. Kains: I move that the Chairman most respectfully bring the matter up to the board at the earliest opportunity, say tomorrow.

Mr. McDougal: I second the motion.

Mr. O. Wells: That does not broaden it.

Mr. Seay: Mr. Chairman, I was convinced, and I am sure that all were convinced, when, without warning, the subject was brought up at the Federal Reserve Board this afternoon, you stated in a very bold and penetrating way, and very briefly, the attitude of this body. I am convinced that the Chairman has the fullest grasp of the situation, and he has that faculty which retains in the mind the expressions of opinions which we have ourselves delivered, and I do not believe it could be more forcefully presented than if he will consent to use the language he used this afternoon and express the opinions he has expressed to us, and incorporate in it that portion of our own opinion that we have expressed as to the feeling of our boards of directors on this subject. I believe that would be the most effective way of presenting the matter to the board, if the Chairman is willing to consent to do so.

The Chairman: Gentlemen, I understand the difficulty or possible danger, or, at any rate, the possible embarrassment, of endeavoring to make a record that expresses the composite views of a number of different people, and then later, a year or two years hence, being required to refer to it as a record. It seems to me undesirable that in a matter of this character we should make a record which would appear to be a commitment of the directors of the various Federal Reserve Banks. If you feel like acting upon the motion that has been made, I will endeavor to express what has been discussed here tonight to the Federal Reserve Board tomorrow in a verbal report, and have the Board understand that that simply is a verbal expression in general terms of the result of the discussion; that we pass no resolution now that might appear to be a permanent record of policy adopted by the directors of all of these banks.

On the whole, I think that is a wise way in which to handle it, if you agree to entrust to me the duty of making that statement, which I will gladly do.

Is there any further discussion of the motion?

Mr. McDougal: Mr. Chairman, I did not make my statement in just the way that I should like to have it appear on the record. In my statement I spoke of the directors, "individually and collectively." I may have done some of them an injustice, because I am not clear as to just how the so-called Government directors did stand in the matter. So I should like to have my statement changed so that all the directors will not be implicated in my statement. I may be doing them an injustice. The matter had been discussed, and I know our directors as a body were very much disturbed because of the fact that they were not permitted to establish rates subject to the later approval of the Board. There may have been two or three of the directors who had no voice in that discussion.

The Chairman: I do not suppose any of us would feel that we were acting here under a resolution of authority from our respective boards of directors. We are simply expressing our own individual opinions of the way our banks, as banks managed by boards of directors, should be represented at this meeting.

Certainly the same condition prevails in every bank, that there are three directors appointed by the Federal Reserve Board who may feel, as a matter of loyalty and duty to their appointing body, that they ought to follow every suggestion that they get from that body. However, I have no hesitation in stating on behalf of our bank that there is a feeling that a mistake is being made, and I regard it as a duty to convey that impression to the Federal Reserve Board. If you are willing to act on the motion that has been made, I will endeavor to make a moderate statement of the matter as forcefully as I can that will represent a composite of the views expressed here; and if any Governor present, hearing what I say, feels that it should be modified or enlarged or changed in any way to meet the situation in his own district, why, I will take the liberty of inviting such a statement after I have concluded tomorrow.

Mr. Seay: To fortify you in your position, Mr. Chairman, I will state in conjunction with my previous remarks, that our board of directors, in framing their official by-laws, which were afterwards changed, gave the power to the executive committee to change the rate for extraordinary reasons. They thereby showed where they expect the control of the rates to lie, and from what source they expected a rate to emanate.

I am sure that I am representing the controlling sentiment of our board. No dissent has ever been expressed when utterance has been given to it. They expect the rates to initiate with them, and they have been very careful in their language, when they have made a rate, and it has been reported that they have fixed the rate themselves. It is something which brings us intimately in contact with our member banks, and when we fix the rate it affects the entire banking business of our district.

I just want to fortify you in your position, sir, as far as speaking for our own bank goes. I do not think you would make any error in stating that.

Mr. Wold: Mr. Chairman, I do not care to qualify the statements I have made. I think they fairly reflect, not a majority vote, but I think they fairly reflect the entire vote, including the Class C directors. In fact our Federal Reserve Agent has, by communication to the Federal Reserve Board, suggested that the rate should initiate with the bank and should be announced from our bank and not from the Federal Reserve Board in Washington. He has a vertebrae.

Mr. Seay: It seems to me, Mr. Chairman, if I am not taking too much time, that my judgment as a banker is that something unsound is being attempted in the effort to equalize rates where conditions vary.

The Chairman: Gentlemen, I am going to ask you whether you will authorize me, in stating this matter to the Federal Reserve Board tomorrow, to refer to one matter which is in my mind as conjecture. I am distinctly under the impression, although I admit that the grounds for it are very slight, that the apparent effort that is being made by the Federal Reserve Board to reduce rates is originated by pressure that is brought upon the Board from outside sources. I do not know what the character of that pressure is, but I just sense the feeling that there is pressure, and that if there is pressure of any kind, the statement should be made before the Federal Reserve Board that if it were known to the management of the Federal Reserve banks or any of them that influences of any kind have been brought to bear in connection with the discussion or decision in this matter of rates, it would be very seriously resented by the management of the Federal Reserve banks.

I admit that that is conjecture; I have no ground for making that statement other than an instinct, possibly; but it is the one thing that this system must be guarded against, and I would not be ashamed to read whatever statement is made to the Federal Reserve Board in regard to the demand that they be absolutely free from any influence whatever in considering the rates; that it should come from the Governors of the Federal Reserve banks; that their duty is to sit there as a judicial body to review what we suggest to them. What we have in fact established at the respective banks is for them to pass upon, and nobody is entitled to go to that board and tell them what they ought to do in suggesting rates to the Federal Reserve banks.

Mr. Kains: I am heartily in accord with that, Mr. Chairman.

Mr. Seay: You have carte blanche, sir, from me.

Mr. O. Wells: Would you not rather say that the suggestions of rates should come from the boards of directors of the Federal Reserve banks rather than from the Governors?

The Chairman: Yes; I spoke in a collective sense there. It is a bad habit that I am guilty of.

Mr. Wold: That is where it comes from, as a matter of fact; it comes from the Governors, does it not?

Mr. O. Wells: No; it comes particularly from the chairman of the board as coming from the board.

Mr. Wold: It does not in our case.

Mr. Seay: I would like to mention something and ask the stenographer not to report it at present.

(An informal discussion thereupon occurred which the stenographer was directed not to report; after which the following proceedings were had:)

The Chairman: Gentlemen, we have a motion. I do not want to hasten a conclusion in a matter of the great importance that this has, but I cannot help but feel that there is such a unanimous expression here as to what our course should be that if any of you now feel disposed to call for a vote on that motion we can conclude this matter, if you will permit me, after this motion is put and acted upon, by making a short statement on the subject.

(Cries of "Question.")

(The motion under discussion, having been duly seconded, was put and carried.)

The Chairman: The statement I would like to make is this: The next likely development of real importance in the matter of rates is to my mind of even greater importance than the one we have been discussing. Just now all the Federal Reserve banks are loaded with money and there has arisen so far and may not arise for some time, no question in regard to a rate of discount to be established for rediscounts between the Federal Reserve banks.

Having participated in the discussion of this bill prior to its adoption, before the Senate Committee, I can assure you that there was no subject that caused greater concern in New York than the possible delegation to an independent body of the right to take some of the assets of the banks of New York and lend them in some other part of the United States without the banks of New York having any right to say whether that loan should be made or not. That matter has not been active in our minds, or in the minds of the member banks, because they are all now laboring under the impression that no situation of that character can arise, at any rate in the near future; but the action that has been taken by the Federal Reserve Board in permitting or suggesting, or at any rate authorizing, a rate of discount in some sections of the country that is lower than the rate which has been authorized by the Federal Reserve Bank in New York and in other districts may result in the accumulation of discounts resulting from the retiring of the Aldrich-Vreeland currency or the spring demand for money in connection with preparation for crop planting, and so on, so as to cause this very situation to arise, that possibly some of the banks in the south or west will get a very large line of discount even to such a point where they may find it desirable to ask for one of two methods of assistance. One is Government deposits; the other, rediscounts.

We have had two meetings of Governors, and I want to tell you that my concern which was an honest one a year or more ago on this subject is just about dispelled. The only remnant of it that is left is this: That I would dislike very much to feel that any Federal Reserve bank felt under the necessity of making application to the Federal Reserve Board for a rediscount with the Federal Reserve Bank in New York.

If any of the Federal Reserve Banks of the South or West reach a point where their resources are getting low, in the interest of the managements of all of the system, I believe it will be highly desirable for that bank to make direct application, either to New York or Chicago, or wherever they may feel it desirable to apply, for a rediscount. I do not mean by that that one of the Federal Reserve banks which may be discounting at four per cent is required to come to New York and rediscount at 4 1/2 per cent and take the loss. The provisions of the Act are broad enough so that the Federal Reserve Bank of New York can establish a rate of discount which will recognize the value of the endorsement of the bank that applies for the rediscount. In other words, with conditions as they are, I would be disposed to recommend in New York that we maintain our present rates for the time being, and that we invite any other Federal Reserve bank that feels it desirable to rediscount any paper to make direct application to us and to permit us to establish a rate for that transaction, which will enable them to rediscount the amount that they apply for at a lower rate than they are receiving on their own rediscounts, and that we in New York will follow whatever procedure we think is desirable in order to make that rate effective.

The object in making this suggestion is this: I know that in some districts there is a large amount of Aldrich-Vreeland currency outstanding. The rate of tax on that currency is increasing. The rate of discount at some of the banks is lower than the rate of tax will be in the near future. If the amount of discounts applied for becomes excessive, I hope that there will be no hesitation in sending word to New York on any ground that rediscount would be acceptable, and I can assure you that if it can be arranged, with or without the approval of the Federal Reserve Board, we will do it. The question has not been submitted to the Federal Reserve Board, and I do not believe that I would care to have it submitted in anticipation of any such transaction; but I think we would feel badly there if we were not permitted to act directly in a transaction of that sort without it being necessary to ask someone in between to make the suggestion for us.

Mr. O. Wells: What is your construction of the law in that respect.

The Chairman: Governor Wells, I do not believe we need to read the words and letters of the law to determine what we want to do. It may be that some obstacle to a direct procedure of that sort will be found, but I doubt it very much. I do not believe it is the intention of the law to require that there should be a board of seven men acting as a broker between the Federal Reserve banks, and I make the suggestion seriously to you, because I think that that is the sound basis on which this business ought to be conducted.

Mr. Aiken: I would like to express my hearty approval of that, and to say we shall be glad to cooperate in the plan as outlined by you.

Mr. O. Wells: I think, Mr. Chairman, representing a section of the country which is more likely, because of conditions existing, to become a borrowing bank than any other sections represented around this board, it would be very pleasing to us to handle the proposition in that manner. We can recognize in it the elements of good sound business procedure, but I believe if this discussion had not arisen at this time, or if I had been making an application, with my impression of the requirements of the Act, that the application would have been made at least in conjunction with some approach to the Federal Reserve Board. Would you not have done so, Governor Seay?

Mr. Seay: Being in a district, Mr. Chairman, which will probably have full use for its resources, I therefore construe your remarks as being somewhat in the nature of an expression of cordial feeling, and I desire to express appreciation of them. I should, however, have taken the course which you have outlined, and applied directly to the Federal Reserve Bank of New York. If there had been any reference to the Board, I think that would come after I had first opened negotiations with you.

(An informal discussion then occurred which the stenographer was directed not to report; after which the following proceedings were had)

Mr. McCord: Mr. Chairman, I deeply appreciate your offer, and that would have been my attitude. I would have first opened negotiations with you or with Boston or Chicago, probably, or some of the districts, a little before I would have taken it up with the Board; and I will do so now if it becomes necessary. I am going to try to drive clear of that. I hope to be able to do so, but in the event that I am not able to do it, I deeply appreciate it and I will certainly communicate with you.

Mr. Kains: I do not anticipate for San Francisco that we will ever be doing that sort of thing, but I certainly think that that is the business way to have this bank managed.

The Chairman: Plural, please, gentlemen.

Mr. Kains: Yes --- "these banks" managed.

Mr. Seay: And "we think."

Mr. O. Wells: Mr. Chairman, while I realize that we are only conjecturing as to what we would have done, it would not have been for the purpose of obtaining it under the belief that that was the means of obtaining it, but it would have been the question of being authorized to discount and of obtaining the rate under which it would be done, and I think decency would have perhaps impelled carrying on negotiations also with the Federal Reserve Banks as to their wishes or as to their desire in the premises. But I still maintain that my natural course would have been to have handled it as a function to be negotiated through the Federal Reserve Board, because of my impression of the reading of this Act, that being the only place in the Act under which we obtain authority to rediscount.

The Chairman: We are hardly under the necessity of anticipating the future in this matter to the extent of taking some action here. I did not want this meeting to be concluded without expressing that view of our interpretation of the meaning of the law. We are prepared to act in accordance with the understanding, and I believe firmly that Mr. Curtis will support us in that opinion.

Mr. O. Wells: Now that the matter has arisen, Mr. Chairman, and supplementing the statement about the Aldrich-Vreeland circulation remaining outstanding in the South to the extent to which it does exist, and the rates tending toward a point that might be attractive as compared with the tax upon the Aldrich-Vreeland Bill, with the further construction that has recently been placed upon the retirement of the

Aldrich-Vreeland currency, which seems to be mandatory by June 30 --- I frankly say to you that in our district the necessity of having between $15,000,000 and $20,000,000 of emergency currency by June 30 being that the problem is upon us for immediate consideration, because we will have no natural liquidation with which to take care of it, of any consequence, between now and June 30, and it is rather imperative that we look towards the retiring of it at some early date rather than waiting until nearly the time set for its retirement under the construction as recorded in the paper this morning, that being a statement given out under authority, as I stated, from the Federal Reserve Board. I am rather of the opinion that it may come up and that it will be discounted only to the extent proper for the retirement of this amount of money, and for taking care of the needs of the season of producing another crop If it can be done without having the interview take a turn of pressing the question, from a practical point of view, or from the point of view of an operation, but simply for our information, if there can be brought out at the interview tomorrow some construction of what would be done under this law, it might be very helpful to us.

Mr. McCord: Do you think that is wise?

Mr. O. Wells: I would like to know what we all think.

Mr. McCord: Do you not think the course suggested by Governor Strong is the best, that we know what the law is ultimately, anyhow; and do you not think it would be better rather than to invite a decision in advance, to let us handle it otherwise, and then if it takes their approval, we can say that we have consulted and it is agreed to? I would rather be put in that attitude than to be put in the other attitude. I would hate to have to go to the Board and let it be said that the Atlanta district had forced New York to do so and so.

Mr. O. Wells: I did not mean that, Mr. McCord.

Mr. McCord: But that would be the result if the decision was against us.

The Chairman: I have no authority for making this statement, but I have reason to believe that the Federal Reserve Board would be very glad to have this matter dealt with in such a way that no such situation could arise.

Mr. O. Wells: I can see no objection to asking for an interpretation of the law, whether we do it as a body or not.

The Chairman: I can see objection to asking the Federal Reserve Board to interpret the law on that point, that is, the paragraph I read under Section 11, which was not taken down for the record, if it gave rise to the amount of hesitation and doubt in the minds of the Federal Reserve Board that arose as to a transaction involving the purchase of gold today --- and I brought the matter up not to ask that any action be taken, but simply to make clear on the record and to you gentlemen what our attitude is in New York. Knowing that attitude, of course you will in each instance follow your own best judgment as to what ought to be done.

Mr. Seay: We first, Mr. Chairman, will have to determine the fact as to whether the inherent right is in the Federal Reserve Bank of New York to make a rate for that purpose. The Federal Reserve Bank of New York might have to reply that "We are willing to do it, but we will have to see what rate we can make you by reference to the Federal Reserve Board."

The Chairman: I think, Governor Seay, if you send us a telegram about such a matter we could get you back a pretty prompt answer about the rate. I think so. I would not say definitely what our Board would do, but I would go so far as to invite you to send the telegram, at any rate.

(I)

Opinions Relative to Right of Federal Reserve Banks to Initiate Changes in discount Rates

A

COPY

Land Title Building
Chestnut-Sansom & Broad St.
Philadelphia

February 16, 1915.

Benjamin Strong, Jr., Esq.,

Governor,

Federal Reserve Bank of New York.

Dear Sir:-

I have heretofore acknowledged receipt of yours of the 11th inst.

I have still further reflected upon the matters about which you asked me to express my opinion, with the result that I have reached a somewhat different conclusion about some of the points and will therefore ask you to treat this letter as my final reply to yours.

It is impossible to answer some of the questions you put without adding that the answers embody a statement of views entertained by counsel in the interpretation of a Statute which inaugurates a new system, and has not, as yet, been sufficiently dealt with by the Courts to afford a reasonable certainty as to what will be their attitude. They may feel inclined to a liberal, or to a narrow, interpretation. Very much will depend upon their point of view.

After the Courts have dealt with the subject, the Federal Reserve Bank Act may, like the Sherman Act, be no longer recognizable by its draftsman.

The opinion which I will express will be one given by me with full appreciation of the fact that other counsel, better able than myself, to construe, may reach an opposite conclusion. What I will say, will not be said in ignorance of the force with which an opposing opinion may be urged.

The Act was intended to bring the banking system of the country as far as possible under a centralized supervision, and, in some particulars, a centralized control. To accomplish this, the Federal Reserve Board was created.

I do not think that an interpretation which does not give a very large measure of power to the Reserve Board, will be sustained by the Courts.

In what I may say as to the method in which the rate of discount is to be determined, I do not mean to include the subject of rediscounting by a Federal Reserve Bank, of the discounted paper of other Federal Reserve Banks.

The Reserve Board is to exercise general supervision over the Federal Reserve Banks and is to "perform the duties, functions, or services specified in this Act," with power to "make all rules and regulations necessary to enable said Board effectively to perform the same."

Supervision does not of necessity include initiation; but this I will specially consider later.

The performance of duties, functions and services involves the idea of more than supervision.

We must therefore examine the Act very carefully in the endeavor to ascertain concerning any special matter, whether the power of the Board is one of supervision or of original action.

Each Federal Reserve Bank, so far as regards the other Federal Reserve Banks, is an autonomous entity; but the autonomies are intended to be brought into as much accord as differing situations and circumstances may permit. The method by which they will thus be brought into accord is the exercise by the Board, of its powers of supervision, and where they are conferred, of original action.

I believe that the Act will be so interpreted by the Courts as will give to the Board such latitude as, consistent with special powers conferred upon the Reserve Banks, will weld the banking system into a harmonious whole.

In the matter of fixing rates of discount, the power conferred upon the Board is that of supervision and modification, not of initiation.

Upon the Reserve Banks is clearly conferred that power of initiation, in this respect, which is essential in view of the fact that rates of discount must differ in different localities. The initial establishment in each locality, of the rate of discount to be charged by the Reserve Bank of the District, can undoubtedly be very much better effected by the Reserve Bank in each locality than by the Reserve Board. On the other hand, the final determination of these rates by each Reserve Bank acting for itself, without any supervision, would make impossible that general harmonization which the Act contemplates.

It is not necessary for me to deal with some of the matters in which there appears to me some confusion, resulting from the fact that at times, probably without any intention to make a change, the draftsman shifted from one word to another. He did not always sufficiently project himself into the future to bring about provisions anticipating what will sometimes occur.

The questions which you put to me, though requiring to be considered in connection with the whole context, involve the interpretation of this particular Section.

> "Every Federal Reserve Bank shall have power **** to establish from time to time, subject to review and determination of the Federal Reserve Board, rates of discount to be charged by the Federal Reserve Bank for each class of paper, which shall be fixed with a view to accommodating commerce and business."

The questions I am asked and my answers thereto, are as follows:-

"1. Does the Act contemplate that rates of discount for commercial paper, shall be initiated by the Federal Reserve Bank only, or by such banks and the Federal Reserve Board, or by the Board only?"

I am very decidedly of the opinion that the initiation of the rates of discount for commercial paper is to be by the Federal Reserve Banks alone. A joint power of initiation by the Board and the Banks, or a power by the Board alone, to initiate, is not conferred.

Most clearly, in my judgment, are the powers of initiation and of supervision, separated, the first being conferred upon the Reserve Banks alone, and the second, upon the Reserve Board.

"2. Irrespective of the general contemplation of the Act, have the Federal Reserve Banks power to establish an effective rate of discount? If so, does it become effective at once upon its establishment and before it has been reviewed by the Federal Reserve Board?"

It is only subject to the review and determination of the Board that the rates initiated by the Banks become effective.

It may be argued with great force that to the Banks is given the power to establish the rates, and that, having thus established the same, such rates go into effect before the Federal Reserve Board has either approved or has otherwise determined upon review.

I think, however, that the establishment by the Banks is not meant to become effective until the Reserve Board has been given the opportunity to review and finally to determine.

Of course the establishment of the rates by the Banks must yield to the exercise by the Reserve Board, of its power of review and determination, and no rates of discount originally established by the

Banks, can be sustained after adverse action by the Board. I think, however, that the rates do not become effective, and cannot be acted upon, immediately upon the establishment by the several banks, before an opportunity has been given to the Board to consider the same.

Most strongly do I advise you not to put into effect any rates which you may establish, until after opportunity has been afforded by notification, to the Board, to exercise its power of review and determination.

The Board itself will probably establish some regulation governing the submission to it of the rates and the manner in which, before they become effective, it will act. Necessarily, such a regulation must be obeyed.

In the absence, however, of any such regulation, I would advise against the making effective, by your Bank, of the rates which it establishes, until after you have become reasonably assured, - the rates having been notified to the Board, - that it does not mean to review.

It is more judicious, however, I think, for you not to act at all, after notification to the Board, until it has notified you of its action in the premises.

The rates can only, in my judgment, be held to have been fixed after establishment by the Bank and review and determination by the Board.

It may be that a failure by the Board, after the lapse of a reasonable time, may be taken as indicative of its intention not to review; but I would not advise action by your Bank on such suggestion.

I therefore answer generally, that I do not think the rate established by your Bank, becomes effective upon such establishment, until it has been reviewed by the Federal Reserve Board and that Board has made its determination in the matter.

"3. If the rate does not become effective prior to review by the Board, does its effectiveness, when it is finally reviewed and approved by the Board, date back to the time of its establishment by the Bank?"

I prefer to answer this question by saying that, until the rate established by the Bank, has been reviewed and determined by the Board, it does not become effective.

"4. May the Federal Reserve Board, in reviewing a rate established by a Federal Reserve Bank, determine that a different rate, not established or recommended by such Bank, shall become effective?"

The power of the Board is not one merely to affirm or reject. The power conferred upon it is to review and determine.

A review carries with it something more than the idea of examining with a view to mere dissent or assent. The word "review" used in connection with the very potent word "determination", convinces me that the review may be of such a character as to involve changes of rates, and that the determination by the Board that such changed rates should be charged, is final and conclusive upon the Bank.

I think the Board has the fullest power to alter and modify rates, and to insist upon its final determination as conclusive upon the Bank.

The review by the Board is not like that which an Appellate Tribunal makes, in the case of a judgment submitted to it upon appeal. In fact, in many cases, the Appellate Tribunal may modify, and does modify, decrees.

Had it been intended to confer upon the Board nothing more than a power to approve or disapprove, the idea, in my judgment, would have been expressed in very different language from that which we find in the Act.

If the Board cannot compel the Bank to accept the rates which it finally determines in review of those established by the latter, what becomes of the power of review? If the Board can merely disapprove, we will have an endless see-sawing between the Bank and the Board.

The rates, in my judgment, which becomes effective, are those which result from the initial action of the Bank, supervised, reviewed and modified by the Board.

In my opinion, the Bank must carry into effect only such rates as shall finally be determined by the Board, in review of the initial establishment by the Bank.

"5. May the Federal Reserve Board review and determine the rate at any time, or is it limited to review such rate within a reasonable time after its establishment by the Bank?"

I see no warrant in the Act for advising that there is a limitation of time upon the Board in its review and determination in the matter of rates established by way of initiation, by the Bank.

Naturally, the Board, if it feels that the Bank cannot act in the matter of rates until it has determined, will feel constrained to act promptly. It is not compelled so to do, however.

I think it may defer, for as long a time as it shall see fit, its action in the way of review and determination, subject to its sense of duty, as to which it alone must be the judge.

It may be that if the Board defers its action for any definite space of time, the Bank may infer that its rates are established;

but I do not advise it so to infer.

"6. What is the effect of the word "determine" in Section 14? Does it mean that the Board may determine a rate and make it effective at any time, for any Bank, without prior action by the Bank?"

In my opinion, the Bank having deferred for such length of time as to it shall seem proper, its action of review and determination, may finally review and determine, and the rate will become effective only thereafter.

In my judgment, no other action is demanded by the Bank after it has established the rate, and the same has been reviewed, modified, if thought wise, and determined by the Board, than to carry the rate, thus finally determined, into effect.

"7. May a rate established by a Bank and reviewed and approved by the Board, be re-reviewed by the Board without any intervening action by the Bank?"

An affirmative answer to this question may be sustained with great force, and my first impression was, that the answer should be in the affirmative.

More careful consideration of the whole Act, and a much more thorough study of the Section I have quoted, however, convinces me that the answer should be in the negative.

I was at first very much impressed by the fact that, if the Board had no power of re-review, there would be a paralysis of action in case the Bank determined to stand by a rate determined by the Board, after it, the Bank, had originally established the same.

This view, however, I am convinced, was too superficial. It lost sight of the very important words "from time to time."

The Bank, at any time, may initiate the establishment of a new rate, subject to the action of the Board in reviewing and determining upon such newly established rate.

Of course, if I am right in what I have heretofore said, the new rate established by the Bank, cannot be put into operation until the Board has acted by way of review and determination. Were it otherwise, the Bank could always set aside the action of the Board by establishing a new rate and making the same effective until the Board should have acted anew in the review of the Bank's later action.

It is the Bank which may "from time to time" establish rates. Nothing is said about the Board, from time to time, reviewing and determining the rates established by the Bank.

The Act, I am convinced, after additional reflection, clearly gives to the Bank the initiative in the matter of establishment of the rate. It makes such rate effective after the Board has reviewed and determined. The rate remains in force until the Bank has acted anew, its action being subject to the reviewing power of the Board.

If the Board, after the Bank has established the rate and after it has acted thereon, may thereafter, under the guise of a re-review, without intervening action of the Bank, establish a rate, the initiative will have been shifted from the Bank to the Board by reason thereof. The Act does not, in my judgment, permit such shifting of power to initiate.

Presumably, the Bank, under changed circumstances, will establish a new rate and will not continue to retain an old one, in order to prevent any further supervision in the matter by the Board.

Different conduct by the Bank is almost inconceivable.

I think we may assume that the draftsman of the Act acted upon the theory that, from time to time, as the Bank should find business exigencies would require, it would establish a new rate, even at the risk that such newly established rate would be modified by the Board in the exercise of its supervisory power.

I am

Very truly yours,

(Signed) John G. Johnson

B

OPINION OF ATTORNEY GENERAL PUBLISHED IN VOLUME 32, PAGE 81
OF OPINIONS OF ATTORNEYS GENERAL

REGULATION OF DISCOUNT RATES OF FEDERAL RESERVE
BANKS BY FEDERAL RESERVE BOARD

The Federal Reserve Board has the right, under the powers conferred by the Federal Reserve Act, to determine what rates of discount should be charged from time to time by a Federal reserve bank, and, under their powers of review and supervision, to require such rates to be put into effect by such bank.

Department of Justice,
December 9, 1919.

Sir:

In response to your request for my opinion concerning the powers of the Federal Reserve Board to regulate discount rates of the several reserve banks, I reply as follows:

By section 14 of the Act of Congress, designated by the short title "Federal Reserve Act" (Act of December 23, 1913, 38 Stat. 251, 264), it is provided that "every Federal reserve bank shall have power -

"(d) To establish from time to time, subject to review and determination of the Federal Reserve Board, rates of discount to be charged by the Federal reserve bank for each class of paper, which shall be fixed with a view of accommodating commerce and business."

By section 4 of said Act each Federal reserve bank is under the supervision and control of its own board of directors, subject, however, to the provision of section 11 of said Act (38 Stat. 261), which provides, in part, that -

"The Federal Reserve Board shall be authorized and empowered * * * (j) to exercise general supervision over said Federal reserve banks.

"The Federal Reserve Board is also further authorized and empowered to examine at its discretion the accounts, books and affairs of each Federal reserve bank * * * and to require such statements and reports as it may deem necessary." (Sec. 11, subdiv. a.)

By section 12 there is also created a Federal advisory council composed of representatives chosen in the manner prescribed in said section, which is to confer directly with the Federal Reserve Board. Among its powers it is authorized to "call for information, to make recommendations in regard to discount rates, rediscount business," etc.

The question for determination is whether, taking into consideration the language of section 14 (d), giving the power to the Federal reserve banks to establish from time to time rates of discount, "subject to review and determination of the Federal Reserve Board," and the further power of the Federal Reserve Board to exercise general supervision over said Federal reserve banks, the power of the Federal Reserve Board is limited to reviewing and approving or disapproving rates of discount made by such banks, or whether said board may, in the exercise of its powers, from time to time review the rates of discount in use and direct specific changes and alterations thereof.

The legislative history of the act shows that as originally drawn section 14, subsection (d), conferred the power upon the Federal reserve banks to make discount rates "subject to review" by the Federal Reserve Board, and that said section was amended in committee by adding the words "and determination" after the word "review," so as to make said section read as now enacted.

It is quite evident that if the Federal Reserve Board is confined to the power to review and approve or disapprove rates of discount made by the Federal reserve banks, and is without power to itself direct specific changes, the words "and determination" are wholly without significance. The very signification of the word "determination" used in such a connection, carries with it the right to pass upon and to decide and fix, and thus determine what should be done. Coupling this with the power given the Federal Reserve Board to supervise the business of each Federal reserve bank, taking also into consideration the recommendations contemplated by the advisory council to the Federal Reserve Board in regard to discount rates, such power would be futile if such Federal Reserve Board could not, if agreeing to such recommendations, direct them to be carried out. I think it is quite clear that the Federal Reserve Board is the ultimate authority in regard to rediscount rates to be charged by the several Federal reserve banks and may prescribe such rates.

This is in all cases necessarily a review of rates existing at the time in the bank, and therefore strictly calls for the exercise of this power. The determination reached by the board carries with it the exercise of the power of determination specified in section 14, subdivision (d), and also exercises the power of supervision granted in section 11, subdivision (j).

The scheme of the entire Act is to have Federal reserve banks in different parts of the country, so that their operations may be accommodated to the business needs of each section, and to vest final power in the Federal Reserve Board, so as to insure a conduct of business by each bank which will not be detrimental to the carrying out of the entire plan. The powers of the Federal Reserve Board are therefore to be exercised in regard to each reserve bank as the conditions surrounding said bank may dictate, keeping in view the general purpose and plan of the Federal Reserve Act. Bearing in mind such general purpose, I am of the opinion that the Federal Reserve Board has the right, under the powers conferred by the Federal Reserve Act, to determine what rates of discount should be charged, from time to time by a Federal reserve bank, and, under their powers of review and supervision, to require such rates to be put into effect by such bank.

Very respectfully,

ALEX. C. KING,
Acting Attorney General.

To the Secretary of the Treasury.

C

C O P Y

WHITE & CASE

14 WALL STREET

JDW.LC New York, February 25, 1920.

Federal Reserve Bank,

120 Broadway, New York.

Dear Sirs:

You have asked for our opinion as to whether under the Federal Reserve Act the Federal Reserve Board has the power to initiate discount rates from time to time, or whether such power resides solely in the Federal reserve banks.

There can be no question as to the power of the Congress. The Federal Reserve Board could have been given the absolute and exclusive power to initiate rates. In fact in subdivision (b) of Section 11 of the Act it has been given the exclusive power to fix the rediscount rate to be charged by a Federal reserve bank on the rediscount for other Federal reserve banks of discounted paper. The question is, therefore, what the Congress intended by the language of the several sections of the Act as to the power of the Federal Reserve Board in connection with the discount rates.

No legal principles seem to be involved in the question except a few simple maxims of statutory construction. The Attorney General in his opinion of December 9, 1919, invokes one of these - that, if possible, meaning must be given to all words of a statute. In applying this principle he emphasizes the use of the word "determination" in subdivision (d) of Section 14 of the Act, wherein it is provided that discount rates as established from time to time by a Federal reserve bank are subject to review and determination of the Federal Reserve Board, and the conclusion he draws, which seems to us justified by the language, is that the power of the Federal Reserve Board is not limited to a review of such a rate but that the Federal Reserve Board may follow such review by a determination establishing another rate, if not satisfied with the one under review. And the Attorney General goes further and holds in effect that the Federal Reserve Board has the power to initiate rates.

The same principle of statutory construction requires, however, that use be made of the words found in the same subdivision giving to every Federal reserve bank the power "to establish from time to time *** rates of discount." Our opinion is that the meaning which must be given to those words is that the Federal reserve banks have the power to initiate rates and, because we find no specific grant of such power to the Federal Reserve Board, that that Board has no such power except in so far as a determination in connection with a review may be regarded as initiation. We think that the Federal Reserve Board's power is, however, spent after a review and determination in respect of a rate established by a Federal reserve bank.

But there is a practical side to the matter. Subdivision (j) of Section 11 of the Act gives to the Federal Reserve Board general supervision over the Federal reserve banks. Those words, which have received some judicial consideration and construction, are broad and effective in their scope and it has been held that an officer who can only advise or suggest to another has no general supervision over him, his acts or his conduct.

Bearing in mind the scope of the power of general supervision, assume that a bank was satisfied with its existing rate, which had already been reviewed and determined by the Board, and assume that the Board had decided that the rate should be changed. The Board might call upon the bank to establish and report its rate, and even though the rate so reported might be the same as before we think there would have been a sufficient exercise of the power of initiation by the bank to open the door for review and determination by the Board.

Or assume that the bank was not satisfied with the rate established by the Board, after review and determination. It might establish a new rate, which also would open the door for another review and determination. Should such a course result in an unseemly race between the Board and a bank to fix the rate, it would, we think, be a fair construction of the general supervision provision of the Act to hold that in such circumstances the Board might direct the bank not to change the rate as determined by the Board until the lapse of some arbitrary but reasonable period, unless some change in the situation "with a view of accommodating commerce and business" (Sec. 14 sub. (d)) should, in the judgment of the bank, have reasonably suggested it - that is, some change from the conditions obtaining at the last determination by the Board. Such instructions would practically tie the hands of the bank, because its directors could not resolve that in their judgment such a change had taken place merely because they thought the rate was wrong. They would in justice to themselves be obliged to believe and find that some such real change had taken place.

We are not commenting on the wisdom or unwisdom of the statute but on the statute as we find it. The history of its passage shows a struggle between the ideas of a central bank and of more or less autonomous regional banks. The latter policy prevailed in general and yet the statute is in several respects a compromise, and the intent is clearly reflected to co-ordinate the several banks through a central power to which is given, among other powers, "general supervision," such absolute and coercive control as the power, on the affirmative vote of five members of the Board, to require a bank to rediscount the discounted paper of other banks at rates fixed by the Board, and the power to suspend or remove any officer or director of any Federal reserve bank.

There are inconsistencies in the statute, as there usually are in statutes that have passed through the fire of compromise between strongly-urged conflicting theories, but the idea of central control, while it may have, in the popular understanding of the statute, been defeated, nevertheless is really the dominant thought of the statute as a whole. As a further instance, it is provided in Section 4 that the board of directors of a Federal reserve bank shall "subject to the provisions of law and the orders of the Federal Reserve Board extend to each member bank such discounts, advancements and accommodations as may be severally and reasonably made with due regard for claims and demands of other member banks." The conclusion seems to us to be clear that the intent of the Congress was, for all practical purposes, to give to the Federal Reserve Board the power, directly or indirectly, eventually to enforce its own views as to discount rates to be charged by the Federal reserve banks.

Our conclusion, therefore, is that the banks alone have the power to initiate rates but that the Board has the power to change those so established; that the Board has no power directly to initiate a rate but that the sweeping power of the Board is sufficient to enable it by one means or another to bring about any changes in the discount rates in any district that its judgment may dictate.

Yours very truly,

(Signed) White & Case.

KMC

J

Copies of Correspondence Relative to Purchase and Sale of Gold and Sterling Exchange.

SENT TO GOVERNORS OF OTHER FEDERAL RESERVE BANKS.

STRICTLY CONFIDENTIAL May 12, 1927.

Dear Governor

We were advised yesterday afternoon that the Governors Conference had authorized the participation among all Federal reserve banks of the gold which we recently purchased in London. A telegram to that effect was immediately sent to you in order that the distribution of the account might be reflected in yesterday's press statement, and I am enclosing a copy of the telegram for confirmation.

I understand that Governor Strong has fully explained this transaction to you at the Conference, and I am now writing merely to confirm the details as a matter of record.

We purchased from the Bank of France on May 6, 89,598.0522 fine kilos (2,880,643.862 fine ounces) of gold, delivered at the Bank of England, London. At the statutory mint price the value of this gold is $59,548,191.54, and we paid for it $59,337,206.05 which, you will observe, gives us a margin of $210,985.49 less than the full mint value. The price at which we bought this gold took into consideration the shipping charges to New York which would amount to about $126,422.85 and also the interest that was saved to the Bank of France by our making immediate payment. Assuming the gold is ultimately brought to New York at current rates the allowance made for interest would, of course, represent profit in which all Federal reserve banks will participate. The item of $210,985.49, pending final disposition of the gold, is being carried in suspense on our books.

Will you be kind enough to write us at your convenience confirming the participation of your bank in this purchase of gold so that our records will be complete.

With kindest regards, believe me

Faithfully yours,

J. H. CASE,
Deputy Governor.

JHC:MK

Sent to all Governors
of other Federals.

STRICTLY CONFIDENTIAL

June 14, 1927.

Dear Governor Harding:

I am writing to confirm the telegram which I sent you yesterday, and to explain in a litt-le more detail the transaction to which it referred.

You have doubtless seen reference in the newspapers to the fact that the Bank of France has been accumulating large balances abroad, particularly in London and New York. We would like to explain our understanding of the situation, which gives rise to the present transaction.

Owing to the flow of funds to Paris heavy purchases of foreign exchange have been made by the Bank of France in order to keep their exchange rate stable. In line with their present monetary policy, it has been the desire of the Bank of France to convert some of these large foreign balances into gold to be held under earmark for them abroad. This has already been done on a considerable scale both in London and New York and, in order to facilitate these large operations, now under way by both the Bank of France and the Bank of England, we have agreed to resell to the Bank of France for payment in sterling the gold which we bought from them last month and which is now earmarked for our account with the Bank of England.

The selling price agreed upon is 84 s. 11 5/11 d. per fine ounce which is the Bank of England's statutory selling price and the equivalent of our mint parity. At the present rate of sterling exchange, $4.85 5/8, there is a potential profit of approximately $85,000, but since we are taking payment in sterling, our actual profit, when converted into dollars, will depend upon the rate of exchange at the time of conversion. With England on a gold basis and on the basis of present shipping costs, the gold import point from London to New York is approximately $4.85. We may therefore consider that as the minimum rate below which sterling will not fall under present conditions. Instead of taking the profit of $85,000 on this sale of gold at this time, however, we propose to use this sum to write down the value of the sterling received in payment for the gold to a price slightly under the gold import point.

The net effect of this transaction will be to convert a non-reserve deposit of gold into earning assets abroad which, when written down by the amount of $85,000 referred to above, will represent a book value below which ~~there~~ their actual value should not fluctuate under existing conditions.

The Bank of England has agreed either to invest the sterling for us in prime commercial bills or else to employ the money at interest as contemplated by our original 1917 agreement with the Bank of England. As you know, the Federal Reserve Bank of New York has at the present time an account with the Bank of England which is not participated among the various Federal reserve banks. It comprises the equivalent of $273,000 in prime commercial bills; $243,000 balance at interest and $341,000 free balance. This side of the Bank of England account has never in the past been offered for participation among the other Federal reserve banks owing to the fact that for some time before England returned to a gold standard there was a loss in the account. While that loss has ceased to exist since England's return to the gold standadd, nevertheless we have felt until now that the amount of the account was too small to justify its participation. As you may remember, this matter has been discussed from time to time with the Open Market Investment Committee and at the various Governors Conferences, when it was understood that until the account increased in size there would be no occasion to offer a participation to the other Federal reserve banks.

In its broader aspects we believe this transaction constitutes a most constructive step in our cooperation with the foreign banks of issue and one which will assist materially in promoting the stability of the gold standard abroad. Our directors have given the matter their most careful consideration and entirely approve of the proposed action.

Will you please be good enough to let us know at your early convenience whether you care to participate in this account with the Bank of England. I am sure that you will appreciate the need for regarding the contents of this letter as most confidential.

Very truly yours,

BENJ. STRONG,
Governor.

Mr. W. P. G. Harding,
Governor, Federal Reserve Bank,
Boston, Mass.

GLH.KMC

COPY

FEDERAL RESERVE BANK OF RICHMOND

June 17, 1927

Dear Mr. Harrison:

Receipt today of the Board's tabulation St. 5405, showing the average rate of current net earnings on paid-in capital of the several Federal Reserve Banks, brings to my attention the fact that this bank is showing earnings upon capital lower than any bank in the System at the present time.

In times past, we have had several methods of distributing System investments, one being upon the basis of capital and surplus, another upon the relation which the earnings and expenses of a particular bank bore to the aggregate earnings and expenses of all the banks, and another upon the need of a particular bank to build up its earnings to meet dividend requirements and certain depreciation charges. It does not appear that adjustment has been made in the plan of distribution since the first of the year, although I believe it has been the practice to make such adjustments heretofore.

We did not join in the general plan of distribution of System investments for the purpose of adding to our earnings, which since the organization of the System up to the present time have been adequate for requirements in the regular course of rediscounting for member banks. Inasmuch, however, as we have joined in participation in System investments, I am calling attention to the fact that, apparently, some adjustment should be made in the present rate of distribution which will meet our requirements. Heretofore there has been an occasional deficiency of earnings in the first six months of the year, usually in the first three months when it occurred, but in the latter half of the year we made up the deficiency. Up to this time, there has been no reason to think that the result of the latter half of the year would not conform to previous experience in making up the deficiency. It is now rather doubtful that this will be the case.

From the enclosed sheet you will see the amount of participation of six banks in System investments in comparison with their capital and surplus. The participation of the Richmond bank is the lowest of any of them and relatively it is much the lowest because the capital and surplus of the Richmond bank is very much in excess of that of any of the other banks specified.

Will you please call to the attention of those who have the matter in charge the fact that some adjustment of distribution is called for?

Yours very truly,

(Signed) Geo. J. Seay

Governor

Mr. George L. Harrison, Deputy Governor
Federal Reserve Bank of New York,
New York City

FEDERAL RESERVE BANK

OF RICHMOND

STATEMENT JUNE 15, 1927
(Even Thousands)

	Richmond	Atlanta	St. Louis	Minneapolis	Kansas City	Dallas
Capital.........	$ 6,206	$ 5,103	$ 5,289	$ 3,005	$ 4,217	$ 4,247
Surplus.........	12,198	9,632	9,939	7,527	9,029	8,215
Total.....	$18,404	$14,735	$15,228	$10,532	$13,246	$12,462

	Richmond	Atlanta	St. Louis	Minneapolis	Kansas City	Dallas
Holdings of:						
Bills Bought in Open Market...	$ 8,329	$ 9,860	$11,427	$ 7,013	$ 9,175	$ 8,629
U. S. Government Securities....	10,342	9,591	28,830	23,015	33,853	26,416
Total.....	$18,671	$19,451	$40,257	$30,028	$43,028	$35,045

NOTE: The earnings of Richmond for year to June 15, 1927, are insufficient to meet expenses and dividends, there being a deficit of $87,383, not including in the deficit the end-of-year charge offs.

COPY

June 18, 1927

My dear Governor Seay:

I want to thank you for your letter of June 17, referring to the present distribution of the System's investments and enclosing a tabulation of the allocation of those investments to six of the reserve banks.

Your letter and the table seem to me to indicate the need of some readjustment but inasmuch as I personally have no contact with the handling of that account, I have discussed your letter today with Mr. Matteson in Mr. Case's absence and learned from him that they are now working on figures and estimates of earnings with a view to making an early redistribution of the account largely because of your own exceptional position. In the circumstances I am giving your letter together with the enclosed table to Mr. Matteson for his information in connection with the work which is now being done in this matter.

I understand from him that while the reallocation of the account is ordinarily not made until the latter part of the year, nevertheless they are considering an earlier readjustment largely on account of your present position.

I am calling your letter to the attention of Mr. Case from whom you will probably hear directly.

Very truly yours,

GEORGE L. HARRISON
Deputy Governor

Mr. George J. Seay,
Governor, Federal Reserve Bank
Richmond, Va.

GLH.KMC

COPY

FEDERAL RESERVE BANK OF RICHMOND

June 20, 1927

Mr. George L. Harrison, Deputy Governor
Federal Reserve Bank of New York
New York City

Dear Mr. Harrison:

I am in receipt of your letter of the 18th in response to mine with respect to the present rate of distribution of System investments, and note that you say this comes more particularly under the jurisdiction of Mr. Case and we will probably hear from him in due course.

Very truly yours,

(Sighed) Geo. J. Seay

Governor

COPY

FEDERAL RESERVE BANK OF BOSTON

June 28, 1927

Dear Governor Strong:

I have received your letter of June 27 with statement showing the gross and net earnings of all the banks for the first five months of 1927 with estimated figures for the last seven months.

It seems to me that the ratio to be used in making distributions of bill purchases is equitable as it is based upon the ratio of earnings required from assets other than Government securities during the rest of the year to cover expenses, dividends and charge-offs.

This is to signify my approval of the plan.

Very truly yours,

(Signed) W. P. G. HARDING

Governor

Mr. Benjamin Strong, Chairman,
Open Market Investment Committee,
Federal Reserve Bank
New York, N. Y.

C O P Y

June 29, 1927

Dear Governor Norris:

I have received your letter of June 28 with regard to future distribution of System purchases of bills, and note that the ratios stated in the memorandum accompanying my letter of the 27th instant have your approval.

Your further comments relating particularly to the item of charge-offs for bank buildings have been duly noted. This is an item which has been rather difficult for the Committee to deal with, but it seems to have been taken care of in a fairly equitable manner and I judge in a manner which is reasonably satisfactory to the majority of the Banks. However, this is a matter which might be brought up at a future meeting of the Committee.

Very truly yours,

Benj. Strong
Chairman, Open Market
Investment Committee

George W. Norris, Esq.,
Governor, Federal Reserve Bank of Philadelphia
Philadelphia, Penn.

C O P Y

FEDERAL RESERVE BANK OF PHILADELPHIA

June 28, 1927

My dear Governor Strong:

I am in receipt of your favor of the 27th instant, in reference to future distribution of bill purchases, and beg to advise you that the ratios used in the third column of the memorandum attached to your letter seem satisfactory, and have my approval as a member of the Committee.

There is but one point, which I have previously made in correspondence and conference with Mr. Case, and which I wish to repeat. That is that it is entirely proper that these distributions should be made with due consideration of the gross earnings of the banks from other sources, and their expenses, dividends, and such charge-offs - furniture, fixtures, and possible losses - as really appertain to transaction of the banks' business, but there ought not to be taken into consideration any charge-off which a bank may see fit to make on its building. If a bank desires to make a large charge-off on this account, and can do so out of earnings from business originating in its District, no other Reserve Bank is in a position to object or criticize, but I strongly object to taking earning assets away from banks which have been economical in their building program to amortize the cost of more elaborate buildings erected by other banks. Such a course is in fact a levy upon some banks to pay for the buildings of other banks.

My recollection is that in 1926 over $2,000,000 was charged off for depreciation on bank buildings. The figures in the statement attached to your letter indicate that charge-offs on this account are likely to be less this year, as the total of charge-offs is only $2,840,000. of which $400,000. is for possible losses in the Seventh District. I am,

Very truly yours,

(Signed) Geo. W. Norris
Governor

Mr. Benjamin Strong, Governor,
Federal Reserve Bank,
New York City

C O P Y

FEDERAL RESERVE BANK OF CLEVELAND

June 30, 1927

Mr. Benj. Strong,
Chairman, Open Market Investment Committee,
Federal Reserve Bank of New York,
New York, N. Y.

Dear Governor Strong:

Your letter of June 27, with enclosures, received. I have carefully gone over the statement of gross earnings and expenses and note the realignment of percentages for the distribution of bills, to become effective in the near future if approved.

I am in accord with the proposed basis, with the condition imposed that the matter will again be studied in September, having in mind that perhaps there should be some adjustment in the percentages as of October 1.

Very truly yours,

(Signed) E. R. Fancher

Governor

C O P Y

FEDERAL RESERVE BANK OF CHICAGO

June 30, 1927

Mr. Benj. Strong, Chairman,
Open Market Investment Committee,
Federal Reserve Bank of New York,
New York, N. Y.

Dear Governor Strong:

Your letter of the 27th instant was duly received, and based upon the exhibits which accompanied the same, the proposed plan for distribution of further purchases of bills seems to be equitable to all concerned, and consequently I have today wired you in accordance with copy of telegram enclosed herewith.

Very truly yours,

(Signed) J. B. McDougal

Governor

C O P Y   O F   T E L E G R A M

CHICAGO 1046A JUNE 30

STRONG

SUBJECT YOUR LETTER 27TH INSTANT, THE RATIOS WHICH YOU HAVE SUGGESTED FOR MAKING FUTURE DISTRIBUTION OF BILL PURCHASES HAS MY FULL APPROVAL AS A MEMBER OF THE OPEN MARKET COMMITTEE

McDOUGAL

1156A

July 19, 1927.

My dear Governor Crissinger:

After a good deal of reflection I am hesitating a good deal about making a trip west. It would be most fatiguing during the hot weather and, as you realize, there is always some possibility of a misunderstanding and other unfavorable reactions.

The action taken by the Board on the recommendations of the Open Market Investment Committee made in May suggests the need for a meeting of the committee the latter part of this month, and I am wondering whether this may not be a substitute for our trip. Would you advise me in reply on what date we could expect to find the members of the Board available in Washington for a discussion toward the very end of this month and I will communicate with the members of the committee to see whether a meeting can be arranged.

Things are very quiet here. Money has shown an easing tendency and we are now making no further purchases beyond the $15,000,000 already reported.

Very truly yours,

Benj. Strong
Governor

Hon. D. R. Crissinger,
Governor, Federal Reserve Board,
Washington, D. C.

(Similar letter sent to Messrs. Norris, Fancher and McDougal)

July 20, 1927.

Dear Governor Harding:

With further reference to our telephone conversation with you today regarding the large holdings of Government securities held by a foreign correspondent maturing on September 15, 1927, and the probable difficulty we will have in replacing them at that time with other short maturities, I am glad to advise you that all members of the Committee have approved of our delivering to this correspondent March maturities from the System Account in exchange for September maturities.

This will afford an opportunity to effect a better distribution of the maturities in the System Account as we are now holding upwards of 81 million dollars maturing March 15, 1928, and a comparatively small amount (about 25 million dollars) of the September 1927 maturity. I have therefore arranged an exchange of this sort of 10 million dollars. It is possible that other exchanges may be made at an early date.

You were also advised that the Treasury is desirous at this time of purchasing a round amount of Second Liberty Loan bonds. They are now difficult to obtain in the market and it is proposed to sell to the Treasury, if necessary, all or any part of the 9 million dollars of that issue in the System Account to be replaced with other short maturities. The members of the Committee have also approved this and we shall be guided accordingly.

Very truly yours,

BENJ. STRONG,
Chairman, Open Market
Investment Committee.

W. P. G. Harding, Esq.,
Governor, Federal Reserve Bank,
Boston, Mass.

LFS.LS

COPY

FEDERAL RESERVE BOARD

WASHINGTON

July 27, 1927

Dear Governor Strong:

This is to advise you formally of the action of the Federal Reserve Board today, following its meeting with the Open Market Investment Committee, in voting that the authority of the Committee be extended for the purpose, a s and when conditions warrant, of not to exceed an additional $50,000,000 of investments.

Very truly yours,

(signed) D. R. CRISSINGER,

Governor.

Mr. Benj. Strong, Governor,
Federa l Reserve Bank,
New York, N. Y.

July 28, 1927.

My dear Governor Crissinger:

This is to acknowledge and thank you for your favor of July 27 advising that the action of the Federal Reserve Board in extending authority to the Open Market Investment Committee to make further investments not to exceed an addition of $50,000,000, as and when conditions warrant.

Very truly yours,

Benj. Strong
Governor

Hon. D. R. Crissinger,
Governor, Federal Reserve Board,
Washington, D. C.

BS/RAH

July 28, 1927.

My dear Governor Crissinger:

This will serve to acknowledge your favor of July 27 enclosing for our confidential information copy of the minutes of the meeting held in Washington on July 27. This report was read to our directors at their meeting to-day, and I may say gave much satisfaction.

We all feel that it was a most enjoyable and constructive meeting, and that the action taken was greatly in the interest of the System and of the country.

Very truly yours,

Benj. Strong
Governor

Hon. D. R. Crissinger,
Governor, Federal Reserve Board,
Washington, D. C.

BS/RAH

PRIVATE AND CONFIDENTIAL: August 15, 1927.

My dear Governor Crissinger:

I am sending you a letter today as Chairman of the Open Market Investment Committee which I think explains itself, but wish to add something to it personally so that you may understand the atmosphere.

There has been a considerable movement of funds away from New York. It resulted as you have observed in the money market remaining somewhat firmer than we had anticipated and it not only resulted in our purchasing somewhat more for open market account than I had expected, but in our doing so much more rapidly than had been anticipated. The transactions reported in my separate letter are simply routine and arose in connection with adjustments made in the various accounts as explained.

We are about facing the need for a very considerable preparation for the September 15 financing. We hold for account of the Open Market Investment Committee and for account of our foreign correspondents something over $200,000,000 of the certificates maturing September 15. If repayment of these were received from the Treasury without any offsetting purchases it would of course result in a very severe stiffening of money rates and a large shortage of reserves in New York, much the largest in fact that we have experienced in some years. In view of this fact we are now proceeding vigorously to purchase several longer maturities against offsetting sales of the September 15 maturities as rapidly as these can be effected. The account will be up and down from day to day, but I want you to understand just what is taking place, and hope you will explain it to your colleagues in the Board.

From this time on I anticipate there may be a fairly steady growth in demands upon us by the money market and we would not wish to have the money situation complicated by failure to anticipate these maturities.

With best regards believe me,

Sincerely yours,

Honorable D. R. Crissinger,
Governor, Federal Reserve Board,
Washington, D. C.

SIMILAR LETTER TO: Geo. W. Norris, Governor, Federal Reserve Bank of Philadelphia
E. R. Fancher, " " " " Cleveland
J. B. McDougal, " " " " Chicago

August 15, 1927.

Dear Governor Harding:

I have today written Governor Crissinger a letter outlining the present status of the Open Market Investment Account. A copy of the letter is enclosed for your information.

As you probably know, there has developed within the last few days a good demand for the new Treasury 3 5/8% bonds, and it has, therefore, seemed a good opportunity for us to carry out the program agreed upon in June; viz., of trading out this $20,000,000 of bonds and acquiring in their place short-term Government obligations. As indicated in my letter to Governor Crissinger, we shall probably dispose of the remaining $10,000,000 of 3 5/8% bonds within the next few days.

We now hold something more than $200,000,000 of September 15 certificates for account of Foreign Correspondents, and for the Open Market Investment Account, which may create a difficult transaction to handle in September. As occasion offers between now and that date, it seems desirable to switch some of these September 15 obligations in the System Account into other short-term paper maturing in December and/or next year.

Do you agree?

Very truly yours,

BENJ. STRONG,
Chairman, Open Market
Investment Committee.

Mr. W. P. G. Harding,
Governor, Federal Reserve Bank of Boston,
Boston, Massachusetts.

Encl.

August 15, 1927.

Dear Governor Crissinger:

At the opening of business this morning the Open Market Investment Account stood at about $301,000,000, with additional purchases made last week, for delivery today, of $4,000,000, which will make the total $305,000,000. This brings us up to a total of $40,000,000 of purchases against the $50,000,000 recently authorized.

This morning one of our foreign correspondents requested us to sell $10,000,000 of September 15, 1927 certificates, which we are taking for the System Account. This will complete our purchases for the present. In addition to this $10,000,000 purchase we have been offered a block of $20,000,000 of the September 15 certificates, and as we hold in the System account $20,000,000 of the Treasury 3 3/8% bonds (for which we turned in Second Liberty Loan 4 1/4% bonds on June 15) which can now be sold to an advantage, it has seemed to us an opportune time to make the switch. We are, therefore, taking in the $20,000,000 of September 15 certificates, against which we will sell the long-term 3 3/8% bonds, and have today sold $10,000,000 of the latter at 100 22/32, for delivery tomorrow. The remaining $10,000,000 will undoubtedly be sold within the course of the next few days.

Very truly yours,

BENJ. STRONG,
Chairman, Open Market
Investment Committee.

Honorable D. R. Crissinger,
Governor, Federal Reserve Board,
Washington, D. C.

THIS LETTER SENT TO GOVERNORS OF ALL OTHER FEDERAL RESERVE BANKS

PRIVATE & CONFIDENTIAL

August 16, 1927.

Dear Governor Harding:

I am enclosing copy of our telegram advising you of the sale of £1,000,000 from the account with the Bank of England in which you participate. You will recall that our purchases of gold in London last spring were made to avoid the importation of gold into this country and that the subsequent conversion of this gold into sterling bills and a balance at interest was effected to aid the Bank of England and the Bank of France in adjusting the Paris-London exchange position.

Since these purposes have now been at least partly accomplished, we have arranged with the Bank of England that our sterling balance may be gradually brought home as and when favorable opportunity offers. The recent strength of sterling exchange afforded us such an opportunity by permitting the sale of £1,000,000 at an attractive rate, namely $4.86-3/32. As this sterling cost about $4.8493, this transaction nets a profit of $11,637.50 but in view of the uncertainty as to the method of disposing of the balance of the account with the Bank of England or the rates at which it might be disposed of, we have thought best to defer for the time being distribution of this profit. We are, therefore, carrying this in suspense for distribution at a later date.

It may be that if sterling continues firm we will make further sales, and we shall send you telegraphic advice from time to time should that occur.

Very truly yours,

J. H. CASE,
Deputy Governor.

Mr. W. P. G. Harding,
Governor, Federal Reserve Bank,
Boston, Mass.

JHC:MK

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Very truly yours,

J. H. CASE,
Deputy Governor.

Mr. W. P. G. Harding,
Governor, Federal Reserve Bank,
Boston, Mass.

JHC:MK

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It may be that if sterling continues firm we will make further sales, and we shall send you telegraphic advice from time to time should that occur.

Very truly yours,

J. H. CASE,
Deputy Governor.

Mr. W. P. G. Harding,
Governor, Federal Reserve Bank,
Boston, Mass.

JHC:MK

f. B

CONFIDENTIAL: August 19, 1927

Dear Governor Crissinger:

Matters are developing from day to day in money market affairs and once more I should advise you just what is transpiring:

In the first place you will observe from the gold settlement fund figures that we have lost over $120,000,000 of our reserves in the last few weeks to the rest of the country. While this is not unusual at the season, I have a feeling, which is shared by some of my associates here, that the movement has been accentuated by the failure of Chicago and Philadelphia to reduce their discount rates. But after all that is a matter for them to decide and we must make our arrangements accordingly.

Until the last day or two the trend of the money market disclosed an underlying strength which disturbed me somewhat, but within the last forty-eight hours it has shown evidence of ease, stock exchange rates today were reduced to 3-1/2%, there is a somewhat lessened demand for Federal Reserve funds, and signs that the commercial paper market has eased a bit as well as the rate on collateral time loans.

One of the results of this ease, of course, is to strengthen the sterling rate somewhat and we have been successful in disposing so far of about £ 3,750,000 of our sterling balances - in round figures about $18,000,000 - This, of course, takes money out of the money market and considering that it involves no change in policy and simply a shift in portfolio from London to New York, we have felt obliged to buy a moderate amount of governments in order to offset these withdrawals.

Taking the situation as a whole, it has worked out most satisfactorily. If we find after the turn of January that our portfolio is larger than necessary we can readily liquidate a part of it. And as matters stand today I think it may be better later in the year to let the needs of the market be supplied by the member banks borrowing from us. The liquidation immediately following the first of January will enable us to judge of the extent, if at all, we should sell government securities.

I hope the whole program has worked out to your satisfaction. I know it has to ours, and our directors expressed satisfaction when the subject was reviewed at yesterday's meeting.

I beg to remain

Sincerely yours,

Honorable D. R. Crissinger,
Governor, Federal Reserve Board,
Washington, D. C.

CONFIDENTIAL August 25, 1927.

Dear Governor Crissinger:

Since my letter of August 16 in reference to changes in the Open Market Investment Account, the strength in sterling has enabled us to make further sales from our London account. Such sales have reached a total of £ 7,180,000 through the close of business tonight, involving the withdrawal from this market of approximately $35,000,000, and up to the close of business last night we had purchased for the System Account, as an offset, a total of $17,004,500 par value of Government securities.

Today one of our foreign correspondents requests us to sell from its holdings $25,000,000 of Treasury certificates maturing September 15 next; of this amount we have purchased for the System Account $15,000,000, making total purchases to offset sales of sterling $32,000,000 and increasing the holdings in the System Account to $347,000,000. The remaining $10,000,000 of these September certificates we have purchased for our own investment account, to be held there temporarily for sale to the Treasury early in September.

With the continued strength in sterling, we will, no doubt, be able to make further substantial sales, in which event we shall continue making offsetting transactions.

Very truly yours,

BENJ. STRONG,
Chairman, Open Market
Investment Committee.

Honorable D. R. Crissinger,
Governor, Federal Reserve Board,
Washington, D. C.

Thomas Newbank

(The following letter sent to Governors Seay, Wellborn, Biggs, Young, Bailey, Talley and Calkins)

CONFIDENTIAL

August 26, 1927.

Dear Governor Seay:

In view of the activity in the System open market investment account and the consequent changes in the Government securities held, it seems desirable to summarize the recent transactions which have appeared in detail in our weekly reports.

On June 9 you were advised concerning (1) the increase in the account from a total of $136,000,000. to $236,000,000. due to purchases made to offset $100,000,000. of gold earmarked for account of one of our foreign correspondents, and (2) the transactions incident to the June 15 maturities in the system account and in the holdings of foreign correspondents.

During June and July additional purchases aggregating $29,000,000 were made under the authority given the committee at the Governors' Conference in May which terminated on August 1st. This brought the total purchases up to $265,000,000. at which the figure remained until recently when an additional $50,000,000 were purchased pursuant to action taken at a meeting of the Open Market Investment Committee held in Washington on July 27, thus bringing the account to $315,000,000.

During the last ten days additional purchases aggregating $32,000,000 have been necessary as an offset to the sale in this market of the System's sterling balances. Sterling exchange since our rate reduction has been consistently strong and it has, therefore, seemed desirable to liquidate a portion of our London account. Up to this date we have sold in round figures £7,000,000. It is probable that further sales of sterling will be made from time to time as the market permits. These sales, of course, have the effect of taking money out of the market in New York, consequently impairing banking reserves, and such security purchases, therefore, are in the nature of offsetting transactions. The total of the system account at the present time is $347,000,000. We do not contemplate further additions to it except as an offset to sale of the sterling balances.

In the meantime some exchanges have been made in the account which have not affected its total. On June 23, $20,000,000. of Second Liberty Loan 4 1/4s were exchanged for a like amount of the new 3 3/8 per cent. Treasury bonds under the terms of the Treasury's offer, and on August 6 these Treasury bonds were sold in the market and a like amount of certificates maturing September 15, 1927, were purchased. On July 8 an exchange of $3,400,000. certificates maturing September 15, 1927, and of $17,000,000. certificates maturing December 15, 1927, was made with other Federal reserve banks for a like amount of Third Liberty Loan 4 1/4s held by those banks outside of the system account. On July 21 we transferred to a foreign correspondent $30,000,000 3 1/4 per cent. certificates due March 15, 1928, and took in exchange a like amount of 3 1/4 per cent. certificates due on September 15, 1927. Since the first of August we have sold in the market $50,000,000. of the September 15, 1927, certificates and purchased a like amount of Third Liberty Loan 4 1/4s.

At the present time we are holding in the system account approximately $75,000,000. of certificates maturing September 15. We are also holding for the account of foreign correspondents approximately $80,000,000. of the same maturity. As opportunity offers we shall make exchange of these certificates for others of a longer maturity, and possibly between now and September 15 it may be desirable temporarily to purchase some additional amounts to be held in anticipation of the September 15 maturity.

The program which has been followed during the past two months has been quite satisfactory from our standpoint and we hope is equally so to you. The only problem at the moment is to make satisfactory disposition of the rather heavy maturities which will occur on September 15.

You will observe that, at least for the present, we have accomplished the important object discussed by the committee at the time of the Governors' Conference in Washington; namely, the accumulation of an adequate portfolio of government securities without placing an undue amount of our funds in the market.

If you have any suggestions in connection with the handling of the account won't you feel free to write me quite frankly.

Sincerely yours,

Benj. Strong
Chairman
Open Market Investment Committee.

Mr. George J. Seay,
Governor, Federal Reserve Bank,
Richmond, Va.

BS/RAH

COPY (sample of telegram sent to Governor of Each Federal Reserve Bank)

August 26, 1927

We have sold from our account with Bank of England further amount of £1,000,000 the cost of which was $4,849,300.00 Your proportion is $ which amount we credit you today. Please apply this credit on your books to account "Due from Foreign Banks-Bank of England Special Interest Account." Details by mail

CASE

Harding, Boston	$ Amounts Listed
Norris, Philadelphia	
Zurlinden, Cleveland	
Seay, Richmond	
Wellborn, Atlanta	
McDougal, Chicago	
Biggs, St. Louis	
Young, Minneapolis	
Bailey, Kansas City	
Talley, Dallas	
Calkins, San Fran.	

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FEDERAL RESERVE BANK

OF MINNEAPOLIS

August 27, 1927.

Mr. J. H. Case, Deputy Governor,
Federal Reserve Bank,
New York, N. Y.

Dear Mr. Case:

Our net earnings today amount to $192,000.00, our dividends, depreciation charges and furniture and equipment amount to $191,000.00, leaving us a bare margin of $1000.00 over and above our dividend and depreciation charges. From now on our rediscounts should decrease as our country banks will be paying us very fast in the next sixty days and, of course, the city banks are only in and out from day to day.

Would it be possible to allot us a somewhat larger proportion of acceptances? I feel that we should have an additional $10,000,000. of earning assets of one sort or another.

I shall be glad to hear from you at your convenience.

Very truly yours,

(Signed) W. B. Geery

Deputy Governor.

C O P Y

August 30, 1927

Mr. W. B. Geery, Deputy Governor,
Federal Reserve Bank of Minneapolis,
Minneapolis, Minn.

Dear Mr. Geery:

I have received your letter of August 27 with regard to your earning requirements for the balance of the year.

With a view to effecting a redistribution of those earning assets which come within the scope of the Open Market Investment Committee, a revision of the allotment percentages has been made based upon the figures recently furnished by all of the banks. The new ratios will go into effect September 1 and the ratio for your bank will be double that recently used. These ratios will, of course, be subject to change should figures to be submitted later indicate further changes are necessary, but provided the earning assets of the system keep up to about their present level, the Committee hopes to be able to distribute them in such a way as to give all banks sufficient earnings to cover their requirements for this year.

I hope this change will be satisfactory to you, but if it should later develop that any further adjustments are necessary we expect to be in a position to make them. As you know, the problem of the Committee is to so distribute the earning assets coming under its direction as to effect an equitable distribution to all banks.

Very truly yours,

J. H. CASE
Deputy Governor

LRR/LAL

COPY

FEDERAL RESERVE BANK OF MINNEAPOLIS

September 1, 1927

Mr. J. H. Case, Deputy Governor,
Federal Reserve Bank,
New York, N. Y.

Dear Mr. Case:

I have yours of the 30th and note that beginning September 1, you will double our proportionate allotment of acceptances. I think this will probably carry us through in good shape and I want to thank you for your action in the matter.

Yours very truly,

(Signed) W. B. Geery
Deputy Governor

SENT TO EACH GOVERNOR OF OTHER FEDERALS

C261

CONFIDENTIAL September 6, 1927.

Dear Governor Harding:

Owing to the weaker tendency of sterling exchange during the past fortnight, we have temporarily discontinued sales of sterling from our balance with the Bank of England. We may, of course, resume again should the exchange strengthen but we are now entering the season when there is normally some pressure on sterling and it may be, therefore, that we shall have to defer further sales for the present.

In any event, we have accomplished our main purpose. You will recall that the gold which we bought in London was sold for payment in sterling and that there was a potential profit in the sale of $85,000 if we calculated the value of sterling at the then existing rate of exchange, say $4.85-5/8. However, we did not take this profit but instead wrote down the value of the sterling on our books to $4.8493. We were thus carrying the sterling at less than the gold import point from London which is about $4.85.

The strength of sterling during August offered us an opportunity to convert our London balance into dollars at an advantageous rate and at the same time permitted us to reduce the Bank of England's liability to us which they were pleased to do without depressing sterling. We have sold £7,525,000 at an average rate of about $4.86-1/8. Since this sterling was carried on our books at $4.8493, there was a profit on the sale of $89,625.92. I think it is advisable to hold this profit in suspense for the present since the London account is not entirely liquidated. We still have £2,435,000 employed at interest, approximately £2,463,600 bills and £77,800 in current account. The money employed at interest yields us 3-7/8% while the bills carry 4-1/4%.

I hope you feel as I do that this account has worked out most satisfactorily not only from the larger standpoint of assisting our European neighbors and improving our own economic and monetary situation but also from the standpoint of profit.

I shall keep you fully informed of any new developments in this account.

With kind regards, believe me

Faithfully yours,

BS

BENJ. STRONG,
Governor.

Mr. W. P. G. Harding,
Governor, Federal Reserve Bank,
Boston, Mass.

JEC:MK

FEDERAL RESERVE BANK
OF BOSTON

C W

September 7, 1927

Mr. Harrison
J

Dear Governor Strong:

I have received your letter of September 6 and note with much interest what you have to say regarding the sales of sterling from the balance with the Bank of England. I think the System is greatly indebted to you for the masterly way in which you have handled this whole transaction and as far as this bank is concerned, I wish to express our appreciation of what you have done.

I am gratified to learn that the Federal Reserve Bank of Chicagohas at last come in line with the discount rate. I presume that Philadelphia and perhaps San Francisco will not lag behind much longer.

With kind regards, I am

Sincerely yours,

W P G Harding
Governor.

Mr. Benjamin Strong, Governor,
Federal Reserve Bank,
New York, N. Y.

J

0261

Mr Harrison

J

FEDERAL RESERVE BANK

OF CLEVELAND

September 7, 1927

Mr. Benj. Strong, Governor,
Federal Reserve Bank of New York,
New York, N. Y.

Dear Governor Strong:

I have your confidential communication of September 6 outlining the handling of the Sterling balance with the Bank of England. It is noted that sales have been discontinued temporarily and that the profit realized from sales already made will be held in suspense.

I know that Governor Fancher will be interested and pleased with your report and it must be very gratifying to you to see this account work out so satisfactorily in all respects.

With warmest regards, I am

Very truly yours,

F. J. Zurlinden
Deputy Governor

Z-D

FEDERAL RESERVE BANK OF CHICAGO

230 SOUTH LA SALLE STREET

OFFICE OF THE GOVERNOR

September 8, 1927.

CONFIDENTIAL

Mr. Benj. Strong, Governor,
Federal Reserve Bank of New York,
New York, N. Y.

Dear Governor Strong:

I have received your confidential letter of the 6th instant, and note therefrom that because of the recent weakness in sterling exchange, you have temporarily discontinued sales of sterling from our balance with the Bank of England.

I also note your reference to the present status of the account and the profits that have accrued to date. I quite agree with you as to the advisability of holding these profits where they are for the present.

It seems to me that the whole matter has been admirably handled; that the desired objectives have been accomplished, and that the results ensuing should be most satisfactory to all concerned.

Thanking you for your advice in the premises, and with kindest regards, I am

Very truly yours,

J. B. McDougal
Governor.

HS.

FEDERAL RESERVE BANK

OF ATLANTA

OFFICE OF
GOVERNOR

September 9th, 1927.

Mr. Harrison

Mr. Benjamin Strong, Governor,
Federal Reserve Bank,
New York, N.Y.

Dear Governor Strong:-

Receipt is acknowledged of your confidential letter of the 6th instant, furnishing us a resume of the handling of the sterling account with the Bank of England.

I fully concur in your feeling that these transactions have been very beneficial from a broad standpoint in assisting our European neighbors, and at the same time helping our own monetary situation. Our responsibility as the world financial center is, in my opinion, being properly borne in the handling of these matters, and I wish to congratulate you on the manner in which this has been accomplished.

We thank you for this information, and desire to assure you of our appreciation of the usual participation by us with your bank in connection with foreign transactions.

With assurances of high esteem, I am

Very truly yours,

M B Wellborn

M.B. Wellborn,
Governor.

W.

W. J. BAILEY, GOVERNOR
C. A. WORTHINGTON, DEPUTY GOVERNOR
J. W. HELM, CASHIER
JOHN PHILLIPS, JR., ASST. CASHIER
E. P. TYNER, ASST. CASHIER
G. E. BARLEY, ASST. CASHIER
M. W. E. PARK, ASST. CASHIER
G. H. PIPKIN, ASST. CASHIER

FEDERAL RESERVE BANK
OF
KANSAS CITY

M. L. McCLURE
CHAIRMAN BOARD OF DIRECTORS
AND FEDERAL RESERVE AGENT
HEBER HORD
DEPUTY CHAIRMAN
BOARD OF DIRECTORS
A. M. McADAMS
ASST. FEDERAL RESERVE AGENT
AND SECRETARY

Mr. Harrison

SEPTEMBER NINTH,

-1927-

Dear Governor Strong:

I thank you very much for your letter of September sixth, in which you fully explain your transactions with the Bank of England, in which this bank is interested. The letter was submitted to our Executive Committee and they join in expressing their satisfaction of your conduct in this matter.

Very truly yours,

W J Bailey
Governor

Benj. Strong, Esq.,
Governor, Federal Reserve Bank,
New York, N. Y.

W. J. BAILEY, GOVERNOR
C. A. WORTHINGTON, DEPUTY GOVERNOR
J. W. HELM, CASHIER
JOHN PHILLIPS, JR., ASST. CASHIER
E. P. TYNER, ASST. CASHIER
G. E. BARLEY, ASST. CASHIER
M. W. E. PARK, ASST. CASHIER
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FEDERAL RESERVE BANK
OF
KANSAS CITY

M. L. McCLURE
CHAIRMAN BOARD OF DIRECTORS
AND FEDERAL RESERVE AGENT
HEBER HORD
DEPUTY CHAIRMAN
BOARD OF DIRECTORS
A. M. McADAMS
ASST. FEDERAL RESERVE AGENT
AND SECRETARY

Mr. Harrison

SEPTEMBER NINTH,

-1927-

Dear Governor Strong:

I thank you very much for your letter of September sixth, in which you fully explain your transactions with the Bank of England, in which this bank is interested. The letter was submitted to our Executive Committee and they join in expressing their satisfaction of your conduct in this matter.

Very truly yours,

W J Bailey
Governor

Benj. Strong, Esq.,
Governor, Federal Reserve Bank,
New York, N. Y.

FEDERAL RESERVE BANK

OF MINNEAPOLIS

September 10,1927.

Mr. Harrison

Mr. Benj. Strong, Governor,
Federal Reserve Bank,
New York, N.Y.

Dear Governor Strong:

This will acknowledge receipt of your letter of September 6 in reference to the disposition of a portion of our free balance with the Bank of England.

These transactions required a little study on my part, which occasioned delay in my replying to your specific inquiry. I believe that the whole transaction has been handled admirably, and our bank wants to thank you for permitting us to participate.

Yours very truly,

RAYoung

R. A. Young
Governor

RAY-C

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PARIS WASHINGTON, D. C.

WHALEY-EATON SERVICE

FOUNDED 1918

American Letter No. 471.

September 10, 1927.

Dear Sir:

1. In our American Letter of June 18 we outlined the developing divergence of opinion in the Federal Reserve System and indicated that a crisis was to be expected. That crisis has developed through the action of the Federal Reserve Board to reduce ~~its~~ Chicago rediscount rate. The issues involved are so fundamental, affecting finance and business everywhere, that this entire Letter will be devoted to the subject. We necessarily give largely the Washington viewpoint.

2. HISTORY: It is not true that this is the first time the Board has ordered a Reserve Bank to reduce its rate. The Board, in 1921, gave an identical order to the Chicago Bank. The latter, however, on the afternoon of the same day, after conference by telephone with the then Governor Harding, requested that it be permitted to "ask for" a lower rate, this to be sanctioned by the Board and to take the place of the "order." This device was employed and the order itself, it is believed, was expunged from the record.

a. In the present case, Chicago submitted the then current rate to the Board, which declined to approve it. Chicago was left for several days without any authorized rate and asked for delay on the ground that a quorum of competent officials could not be got. The Board refused to permit delay on this account and, after notifying the Chicago bank to that effect, took action on its own account.

b. Similar pressure had already been brought on the San Francisco bank, the Board declining to sanction a continuation of the old rate. The only difference was that San Francisco technically asked for an approval of the lower rate as if the action were voluntary, whereas Chicago refused so to do.

c. The policy of easing the money situation was adopted at the conference of central bankers in New York, in July. The plan, before adoption, was submitted to each of the 12 Federal

Reserve Banks. It was accepted by 11 of them, Chicago objecting.

3\. AUTHORITY AS TO RATE: As to the authority of the Federal Reserve Board to order a particular rate, it is not believed that Senator Carter Glass, "Father of the Federal Reserve Act", is correctly reported as being dubious. There is on record a letter written by Mr. Glass, in 1919, to the Attorney General, wherein he states, we are told, that he not only concurs in a legal opinion favoring the Board's authority, but adds that the opinion by counsel "could have been made even stronger had he known the facts as I know them," and urges, we are advised, that unless the Board did have complete power to fix rediscount rates, "it would be powerless to control operations of any regional bank in the System which might engage in transactions perilous to the entire System and to the commerce and industry of the country." And Mr. Glass was the more insistent on this point because, he pointed out, the authors of the Act realized that rate-making might, and frequently would, affect the commerce and industry of the whole country. Official Washington is entirely convinced that there is no doubt as to its legal authority in the premises. It looks for political, not legal, attack, meaning that the issue is not one for the courts, but for the people, to decide.

4\. MOTIVE: The Federal Reserve Act specifically provides that discount rates "shall be fixed with a view of accomodating commerce and business." There is a powerful element in Washington which takes the following view:

> It is mandatory that rates be fixed to accommodate commerce. The movement of crops is commerce. Therefore, when crops are to be moved, instead of money rates hardening, as they have done in the past, they ought to be put at the lowest possible figure. It ought to be fundamental national policy, and it is believed the Federal Reserve Act so directs, that annually, in crop-movement time, the Reserve System should be used to ease the situation. Discount rates, in normal circumstances, should be lowered every Autumn.
>
> This year there were abnormal and compelling circumstances. The foreign central bankers were quite frank in declaring that they could not of themselves handle prospective American crop purchases this year. They insisted, however, that if

American rates were such as to attract bills to New York, New York thus bearing the burden, Europe could fill her entire crop requirements, and do so soundly. On the other hand, Britain, in particular, could not maintain the gold standard and purchase in volume in America also.

The "easy money program was adopted, therefore, for one purpose and one purpose only, namely, to assure European purchases of American crops under facile conditions. The domestic factor was the determining factor absolutely."

"It is idle to talk of helping the farmer by new legislation if we do not use the legislation we already have. What good to grant him subsidies or any other aid if every Fall we raise obstacles against the free movement of his crops to market? He is entitled to have the Reserve System used for his benefit, as it is used for the benefit of all other industry, and that is how it is now being used."

5. CENTRALIZED POWER: The broad issue raised is as to whether or not the Federal Reserve Board is to have the equivalent powers of a central bank in fixing discount rates. We are told that in the Glass letter previously referred to the statement is made that it was the intent of the authors of the Act to enable the Board to exercise a power on discount rates throughout the country "tantamount to the power exercised over the money market by the Bank of England." We get this point of view:

There is certain to be centralized control. The only issue is whether that control shall be through the New York Bank or through a Board in Washington. In one case, there is private control and in the other there is partial Government control.

The System is now regional only in the sense that the regional banks issue currency and do discounting. There must be centralized control. There is such control. Were there not and could American finances not be mobilized, were no consideration given to world requirements, as affecting maintenance of our foreign markets, this country being the world's capital reservoir, a disaster comparable to that of the deflation period would ensue. In these circumstances, it is essential that the Board have complete power. That is the practical aspect, and any discussion otherwise must be academic.

6. POLITICAL PHASES: It is believed in Washington that the Thompson anti-foreign campaign in Chicago has affected the attitude of Chicago financiers. It is also believed that the present incident, which gives the appearance of an American financial policy having been dictated abroad, will give the Thompson elements a

strong position before the people, which even the agricultural feature responsible for the policy may not overcome. It may fire anew the old Anti-League issue, and thus be determinative not only of the Presidential candidate to be named by the Republicans but also of the election.

a. It is well known in Washington that Mr. Mellon's first choice for the Republican nomination is Calvin Coolidge, if he can be persuaded to accept, and his second choice Mr. Hughes. The movement for Mr. Hughes is already far developed in important business and other quarters. But Mr. Hughes has been taking a broad view in international matters. He would hardly fit into a Republican campaign a chief feature of which would be to win the Middle West on an anti-foreign platform.

b. It comes more and more to be accepted in Republican circles that Smith will be the Democratic nominee. "Is it better to bid for the whole Middle West and figure on winning without New York or to run the risk of losing some of the Middle West and winning in New York?" In other words, which is safer, a Middle Westerner or Hughes (Coolidge)?

A fight on the Reserve System which developed a sectional issue would complicate the whole political situation.

7. QUARRELS: It has been the practice of the Administration to try to prevent, within reason, public quarrels on economic issues, as in the case of Eastern railway mergers where the executives have been urged to get together and solve their own problems. It is feared that if the bankers now permit a banking issue to go to the polls, as they did mistakingly in Jackson's time, there will be trouble ahead. Other issues automatically subordinate themselves to a banking fight, when the question is fundamental. An effort may be made, when the Federal Advisory Council meets next week, to reach some sort of accommodation, or at least to postpone a general fight until after the Presidential elections. The Chicago position, however, will have formidable support and not even New York is inclined to acquiesce in far-reaching powers for the Board.

8. PERSONNEL: Criticism of the personnel of the New York bank administration is not taken seriously . "We do not see how Governor Strong could safely be replaced just now." As to the Board itself, there are to be vacancies in several of the independent commissions and the Board is not considered as immune to changes. If there are any, however, this situation will not have caused them.

9. The very vitals of the Administration's policy, as developed over the past few months, is the stimulation of business through the Federal Reserve System, and otherwise. The Treasury operations of this and other countries are based on the promise of cheap money. There will be no change of policy, as will be shown when the Minneapolis rate drops. The outlook, therefore, is for a continuation of stimulating influences. Moreover, the influence of Mr.Mellon, "the optimist", has made Washington even more confident that business over the Fall is to be good. Not much importance is attached to complaints of commercial banks that the "easy-money" policy imperils their ability to make earnings.

WHALEY-EATON SERVICE.

PARIS

WASHINGTON, D. C.

WHALEY-EATON SERVICE

FOUNDED 1918

FOR CLIENTS ONLY

Foreign Letter No. 439.

September 13, 1927.

Dear Sir:

1. There is apprehension in Europe lest the controversy between the Federal Reserve Board and the Chicago Reserve Bank may lead to a political campaign, similar to that over the League of Nations, and thus destroy, or tend to destroy, the delicate equilibrium of international finance. We get, in substance, the thoughts of a gentleman who participated in the New York conference of last July, where the policy of easing credit was accepted.

> We presented no ultimatum to the American authorities. They had their own complete reports of the situation and did not need our observations to guide them. It was a simple matter of arithmetic to show that the maintenance of the gold standard in Europe was out of the question unless America intended to perform her proper function as the credit capital of the world. She was asked to do nothing that Britain has not done a dozen times, as a matter of course, in the days of her financial supremacy. Even so, the deciding arguments came from domestic American considerations, particularly facilitation of crop movements. It would be unfortunate if the contrary were believed in the United States.

There is reason to believe that the foregoing is a comparatively mild statement. It is no exaggeration to say that the situation described at the New York Conference was one of intense seriousness. So much so that such expressions were used as "a collapse possible within a week", etc., etc. London is not alarmed over the present outlook, since there is no possibility of a change in the agreements entered into in July. Adoption subsequently of a provincial attitude on finance by the United States would have far-reaching and disastrous results, it is believed.

2. COMPULSORY ARBITRATION: It is admitted in diplomatic circles that Stresemann's acceptance of the principle of compulsory arbitration will assume larger im-

Mr. Crane

PARIS

WASHINGTON, D. C.

WHALEY-EATON SERVICE

FOUNDED 1918

FOR CLIENTS ONLY

American Letter No. 472.

September 17, 1927.

Dear Sir:

1. It is probable that, within 30 days, the Florida Citrus Exchange will formally make an offer which Secretary Jardine will accept, resigning from the Cabinet. The negotiations, so far, have been through intermediaries, wherefore "denials" have been technically correct.

> Mr. Coolidge has returned from the Northwest pretty well convinced that some sort of farm relief is imperative. It is indicated that he would favor naming a new Secretary of Agriculture who would personify a positive farm legislative program, as an alternative to the McNary-Haugen proposal.

2. APPOINTMENTS: In addition to the vacancy on the Federal Reserve Board occasioned by the resignation of Governor Crissinger and the foregoing probable vacancy in the Cabinet, the President will be called on to make appointments to two or three other of the independent commissions, by reason of resignations. It is indicated that some of the bitterest fights in the Senate will be waged over some of these appointments.

   a. Although farm-organization leaders are saying publicly that they are "open-minded" as to the confirmations of Messrs. Meyer, Cooksey and Harrison as members of the Farm Loan Board, they are actually antagonistic. Their complaint is not so much against Mr. Meyer personally as against the fact that two of his intimate subordinates were appointed with him,"the effect being to give one man three votes on the Board." There is complaint also about Mr. Meyer's optimistic forecasts as to farm income for this year, it being urged that such forecasts are not part of his job and are not accurate. The Administration, on the other hand, feels that Mr. Meyer has read order into the situation and that his record of achievement will be decisive in his favor.

3. FEDERAL RESERVE POLICY: The resignation of Governor Crissinger, it is indicated, will occasion no change in broad Federal Reserve policy. On the contrary,

that policy may be strengthened in its essential details, which are: (1) Assertion of America's world financial supremacy by courageous performance of the functions this entails, including active cooperation with the central banks of other nations; (2) Use of the System actually to accommodate business by fixing rediscount rates with that end in view, with particular reference to facilitating crop movement every Fall and enabling Europe to buy surplus crops; (3) Full concentration of the nation's financial reserves, a step in which direction was taken by the enactment of the McFadden measure at the last session of Congress. The theory underlying (3) is that finance, like man-power, is the first line of the national defense, and must be ready for immediate mobilization. It may be stated authoritatively that Treasury requirements were not determinative as to the present cheap-credit policy. Moreover, the policy was decided on in connection with the July conference of world central bankers, is in the nature of a definite engagement and could not be changed without breach of faith. Therefore, it will not be changed until the engagements have been carried out, which means that a stimulating financial policy will continue, in the absence of unexpected developments, over the next few months.

a. Governor Crissinger has been the outstanding "farm member" of the Board, although not appointed as a farmer. His sympathies throughout have been with agriculture, he having personally experienced its difficulties through his own farm operations.

b. An accommodating spirit has been shown in an effort to patch up the Chicago affair. Apparently it has gone too far, however, for the issue to be avoided in Congress, where a real battle is forecast. It will center, in the House, around the Strong bill, which directs the Board to fix rates so as to stabilize prices.

c. The delicate feature of the situation concerns the weight given to international requirements in fixing Board policies. Unquestionably the British situation was a major influence in fixing the discount policy now in effect. Frank statements that Britain would have to abandon the gold standard, unless aided, were made. This opens a field for political activity. The Thompson elements, of Illinois, in all their conferences as to a Republican Presidential nominee, have laid it down as a sine qua non that the man they support must be 100% anti-League and 100% anti-internationalist. It is stated as a truism abroad that should the United States refuse to cooperate in stabilizing world finance, new debt settlements would become almost immediately requisite.

4. TARIFFS There appears to be an idea in Europe that the American tariff barrier can be crossed through the negotiation of treaties, on the theory that a treaty is supreme law in the United States and would over-rule a mere tariff law. The Administration is utterly hostile to any such device.

a. Section 317 of the Tariff Act directs the President to levy "new and additional duties" against foreign nations which discriminate against American commerce. The Administration reads this as a mandate to negotiate most-favored-nation treaties only. Four such treaties have been negotiated, those with Germany, Hungary and Esthonia being in full effect, while that with Turkey has not been ratified by the Senate. Fourteen such treaties are in process of negotiation, with Norway, Sweden, Finland, Latvia, Poland, Switzerland, Austria, Serbia, Czecho-Slovakia, Honduras, Guatemala, Salvador, Brazil and France. A most-favored-nation clause appears in the modus-vivendi agreements under which commerce is now carried on with Albania, Brazil, Dominican Republic, Finland, Greece, Guatemala, Haiti, Latvia, Lithuania, Poland, Rumania, Turkey and Spain. With all other countries (except Cuba which has special reciprocity) old treaties of various kinds are still operative.

b. There is no important nation, it is felt, that can afford to enter into a trade war with the United States. France and other nations might be able to gain some concessions in the administration of certain laws, outside the Tariff Act, which burden their commerce with America. It is intimated that this may be an object of the present French strategy.

c. Dominant factors in the Tariff Commission rather welcome the Argentine refusal to permit American agents to investigate production costs, a system which has caused much trouble and hard-feeling. The alternative is "United States Valuation", and that is what elements which formerly demanded "American Valuation" will fight for in the next tariff measure. The French agitation has not strengthened the hands of those who want a "trading feature" in the next tariff bill.

d. The Tariff Commission has just completed final revision of its Dye Census for 1926. Copies should be ready for distribution about September 23.

The volume of tariff matters reaching Washington is growing rapidly and indicates that the country is getting ready for tariff revision. The next session of Congress will lay the ground for this as an issue in the Presidential campaign.

5. TREATIES: A significant view as to treaties is furnished by a high authority:

> Treaties are no longer political; they deal with commerce almost entirely. More and more, our commercial policies will have to be determined through treaty provisions. Manifestly this will be impossible, in practical politics, if treaties continue to be made by the Chief Executive with the sanction of the Senate only. There will have to be a constitutional amendment providing that treaties shall be subject to approval by both Houses of Congress and that a majority vote shall be decisive in each House.

6. "NO PROFITS": The article, "Prosperity but no Profits", in the Nation's Business, has been enthusiastically praised by numerous manufacturers who claim that they are being forced to accept non-profitable contracts "by the tyrannical methods of purchasing officers of large corporations." The official view is that Washington can do nothing about it and that the motor industry, in particular, will have to solve this problem for itself.

7. BOLSHEVISM: In advising business leaders not to contribute to organizations soliciting funds with which to combat Bolshevism, the adviser on public relations to some of the most important American financial interests takes this view: "The best way is to let the radicals talk themselves to death. They are not fooling American workmen who know a gold brick when they see one." This is in contrast to the great number of letters reaching Washington protesting that Bolshevism is active and should be watched carefully.

8. CONSOLIDATIONS: Work on the Parker railway consolidation bill has been going on all summer. It will be introduced so soon as Congress convenes. Quick committee action is not yet assured, but it is <u>hoped</u> final passage will be got. It is understood to be the position of the Interstate Commerce Commission that "legislative removal of some existing impedimenta" to mergers would be helpful.

9. The political situation continues to be confused. Professional Republican leaders are in doubt which way to jump. They are confused by statements, said to have been made by the President himself, that Fess or Hoover would do, and they cannot tell how far the Hughes situation has actually developed. Neither are they by any means convinced that Mr. Coolidge is out of the picture. Admittedly, however, active support of any candidate by Mr. Mellon would be almost decisive. Reports continue to flow in of the increasing strength of Smith and of the practical manner in which his campaign in the provinces is being conducted.

WHALEY-EATON SERVICE.

TWO VIEWS OF EUROPE.

(Pamphlet Vol. II. No. 24 - Now Ready.)

The text consists of two private letters to Whaley-Eaton Service. The first of them is written by an American who knows Mussolini intimately. It quotes the Duce on such subjects as the Sacco-Vanzetti case and gives the "strong-government" view of conditions. The other letter, much shorter, is written by an authority who has been in intimate touch with European industrial leaders all summer and who denies that there is any substantial anti-Americanism in business circles abroad.

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The price for single Pamphlets is 25 cents each. Those who have not placed a blanket order for all Pamphlets, as issued, will find the form below convenient for ordering Pamphlet No. 24.

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Whaley-Eaton Service,
Munsey Building,
Washington, D. C. September ___, 1927.

Please mail to the following address ___ copies of "Two Views of Europe."

The price is twenty-five cents the copy. Charge to my account.

(Signed)______________________________

(Address)______________________________

Extra copy

September 19, 1927.

My dear Harding:

You have been good enough to send me a copy of your letter to Governor Seay dated September 14, and I have just received yours of September 16 addressed to Mr. Platt. I am sending you a copy of a letter which I wrote to Governor Seay and one which I am to-day addressing to Secretary Mellon.

With most of your letter of September 16 I am in entire accord, but there is one point where I think we take a different view of the meaning of the Act which you will find discussed in my letter to Secretary Mellon.

If Congress intended that rates should be initiated only by the directors of the Reserve banks, that when initiated they should at once become effective, and that the right of review by the Federal Reserve Board was not simply the right of review of that particular change when it must with reasonable promptness be approved or disapproved, then the language of the Act is indeed very inept in expressing any other intention. For instance, if as suggested in your letter, the Board should accept the decision of the directors of any reserve bank, permit the rate to become effective and continue for, say, a year, then exercise its right of review, and, after reviewing, determine to change the rate, obviously the right of review is continuous from the day the rate is changed until the Board in its discretion decides itself to initiate a change, and the Act could readily and clearly have expressed that intention in other language so clear and unmistakable that the language that it did employ could hardly be accepted as containing that meaning. My own opinion has always been that the compromise expressed in this language left out of account certain possibilities which have, in fact, arisen from time to time, and it is those very possibilities which cause the trouble.

Those, I think, are first, where a rate is established by a reserve bank which is either an increase or a decrease too great at the moment to be justified, and where the Board, desiring to increase or decrease the rate, decides that it will do so but not to the extent proposed by the directors of the Reserve bank. In that event, would the Board have the right to disapprove the rate submitted but to establish some other rate different from the one which had then been in operation?

The second possibility is the question which has arisen in Chicago, where the directors decline to make a change but re-submit the old rate. There is no formula in the Act to determine whether the re-submission of the old rate by the directors of the Reserve bank gives rise to the right of review, and if so, whether the Board has the right then to establish some different rate after disapproving the continuance of the old rate.

Third, except for these two possibilities I see no chance of misunderstanding as to the meaning of the Act, and cannot read into it the intent that the right of review should be continuous. You mention the provision of Section 11, paragraph (b) as sustaining your view. I think it more nearly sustains the view expressed in my letter to Mr. Mellon.

I had intended to telephone you about this matter last week, but was so busy that I did not get around to it. You have given such a whole-hearted support of the program adopted last July that I am most anxious you should not misunderstand our position in New York. We have not wished to intervene in the controversy between the Federal Reserve Board and the Federal Reserve Bank of Chicago, and, in fact, have scrupulously refrained from doing so from the very beginning, with one exception. When I learned from Governor Crissinger that the Board proposed to take the action that it did take, I expressed a strong hope that they could be persuaded not to do so, and on the eve of their action I had opportunity to talk it over with Secretary Mellon and had hoped that his own wishes in counselling delay until he reached Washingtou would prevail. Unfortunately, the Board had already acted when I communicated this to Governor Crissinger.

I am sure you will also recall that when we submitted the proposal for a reduction in New York and asked the views of the members of the Open Market Investment Committee, I was careful to state that we would not make any recommendation as to rate changes in other districts, that what we wanted was their reaction as to a change in our rate, and according as might be decided at the meeting we would either reduce first, or if others preferred to reduce first we would wait until they had opportunity to take it up with their directors.

I do hope this matter can be dealt with so as to avoid either litigation or appeals for amendment.

Many thanks to you for sending me the letter.

Sincerely yours,

Mr. W. P. G. Harding,
Governor, Federal Reserve Bank,
Boston, Mass.

BS/RAH

Extra copy

September 19, 1927.

My dear Mr. Baker:

It is good news to learn that you are expecting shortly to be in New York, and I hope you can spare the time for a visit with us.

Knowing how interested you must be in recent developments in our affairs, I thought you might be able to spare the time for a little chat about that also.

The question of the authority to initiate changes of discount rate has been the subject of a difference of opinion within the System and, at times, of some dispute, from the very beginning. As is so often the case this arises from inept language in the statute, chosen as the result of compromise of opinion, and possibly deliberately ambiguous so as to be capable of construction to meet different views.

The whole question revolves around the meaning of Paragraph (d) of Section 14, and would probably boil down to a decision as to whether the establishment of rates "from time to time" by the Reserve banks offers the occasion for a "review and determination" when changes are made only, or whether that review is continuous and may be exercised at any time after a rate is established and result in the initiation of a different rate as the result of that review.

I have never felt that Congress intended that the Board should have that power, partly because it would have been so simple to have expressed it differently in language of unmistakable intent, and partly because it seems to be inconsistent with the provisions of Paragraph (b) of Section 11. Would Congress have required five votes out of seven (the number of members of the Board originally provided) in order to require this occasional and comparatively unimportant act, and then permit a bare majority vote in order to require a Reserve bank to change its discount rate which is the most important act it performs?

There are certain general provisions in the Act of supervision, regulation and control which have been construed by those previously rendering opinions as giving the Board this power, irrespective of this specific question of Section 14, and there is still another view occasionally expressed that the general powers of the Board could be exercised to require a change of discount rate by some one or two reserve banks which were recalcitrant in conforming to a general System policy. However this may be, and whatever Congress may have intended, I deplore the whole thing and believe it is unnecessary and likely to do us an immense harm unless understanding can be arrived at which will be sufficiently satisfactory to escape a lot of legislative tinkering with the Federal Reserve Act.

Frankly, what I fear is something which has never as yet arisen within the Federal Reserve System, and which may be precipitated by this controversy. I have had occasion more than once to appear before Congress in order to make explanations of various matters connected with the System, and they have in each instance been the result of criticism by the public or by members of Congress or by others outside of the System as to some particular things that we have done. If Congress inquires into this matter in connection with attempts to amend the Act it will involve the appearance of various members of our own organization who hold contrary opinions on this subject, and the country will be concerned lest internal war lead to a situation in which the whole country mighty suffer. Congress assembles in less than three months. Between now and then it seems to me we must find some formula and publicly announce it so as to avoid discrediting ourselves by giving evidence of internal dissension.

I am really distressed beyond my power to express it. It is so discouraging after these thirteen years to feel that we may all be victimized by this silly and wholly unnecessary and, one might even say, quite gratuitous advertising of differences of opinion between men of mature experience who should be capable of more foresight than has been exhibited in this matter.

Now, I have let off this steam, and it has done me good. When you come to New York I will tell you all about it.

You will be interested to know that I had quite a visit at Tuxedo with Mr. George F. Baker a few weeks ago. He inquired particularly about you, and as I found him interested in his old age in reading something about the Constitution of the United States, I have sent him a copy of your book.

With best regards,

Faithfully yours,

Hon. Newton D. Baker,
Union Trust Building,
Cleveland, Ohio.

BS/RAH

Extra copy

September 19, 1927.

Dear Mr. Secretary:

You may not have understood my comments upon the suggestion of obtaining further opinion from the Attorney General in regard to the right of the Federal Reserve Board to initiate changes of discount rate, as the telephone connection was not satisfactory. The points I desired to make were the following:

First, it has been stated to me that it is the practice of the Attorney General not to review opinions rendered by his predecessors in office, but always if possible to rely upon former opinions such as the one rendered by Solicitor King on this subject in 1919.

Second, if this practice prevails and he should either decline to render another opinion giving a different interpretation of the law, or should adopt the opinion of Solicitor King as the view of the Department, the only alternative protest resting with the Federal Reserve Bank of Chicago would be either to resort to the courts or to attempt to secure anamendment to the Act. As either of these courses, it seems to me, might be quite unsatisfactory in their consequences because of the widespread agitation, I had hoped that some other method of adjusting the difficulty would be found possible.

Third, if the practice referred to above does not prevail and the Attorney General should render a new opinion, then a further difficulty lies in the very circumstances under which such opinions are usually sought. The one requested by former Secretary Glass in 1919 was, we understand, the result of a difference of view between Secretary Glass and his associates in the Treasury and the Federal Reserve Bank of New York, the latter having with increasing urgency advocated advances in discount rates throughout the year 1919. The submission of the question at that time was in the form of a letter addressed to the Attorney General by Secretary Glass, accompanied by an opinion of Special Counsel Elliott which we are advised urged the Treasury's point of view. The position of the Federal Reserve Bank of New York as to the true intent of the law and as to the facts of the situation at that time was, of course, never presented to the Attorney General. The year 1919 was one of very serious strain upon our credit resources at a time of feverish speculation in both securities and commodities. A very large expansion of bank credit was taking place, and we were facing the probability of large exports of gold following the removal of the embargo. On the other hand, the Treasury had a floating debt of over $6,000,000,000 and contemplated a large refunding loan of possibly $6,000,000,000 in the fall of that year. There was, in fact, almost a national emergency in the fall of that year. It is only fair to remember that the Attorney General's opinion was rendered in that atmosphere.

Fourth, at the present time the circumstances are quite different. There is no national emergency, the action of the Board in forcing a reduction of rate in Chicago can hardly be sustained upon that ground, and a review of the Act to determine the true intent of Congress should, it seems to me, be undertaken judicially, without any influence such as might have been important under the circumstances prevailing in 1919. Indeed it has been suggested by some of our directors that this difference in circumstances between 1919 and 1927 might possibly make the basis for an opinion limiting to an emergency whatever rights the Federal Reserve Board may have to initiate rates.

Fifth, the officers and directors of the Federal Reserve Bank of New York have never agreed to the interpretation given by Solicitor King to Section 14 of the Act which provides "every Federal reserve bank should have power * * * (d) to establish from time to time, subject to review and determination of the Federal Reserve Board, rates of discount to be charged by the Federal reserve bank for each class of paper, which shall be fixed with a view of accommodating commerce and business." This language appears to be appropriate to what would undoubtedly be the practice of the Federal Reserve System. Rates, according to changing circumstances, should be subject to change by the different Reserve banks "from time to time." These changes of rates made at recurrent periods should be subject to "review and determination by the Federal Reserve Board." If the Board failed to approve changes made from time to time it would obviously have the power to veto any change under this language. But the Act is not clear on two or three points, namely, (a) in case the Board disapproves a change of rate established by a reserve bank, can it fix some other rate, or must it simply require the old rate to continue? (b) is the right of "review and determination" a continuous right or does it only arise "from time to time" as new rates are established by a reserve bank.

It has always seemed to us that when a Federal reserve bank submits a new rate, that rate becomes effective from the moment of its establishment by the Federal reserve bank and approval by the Federal Reserve Board. We do not believe that the Board once having approved of the new rate could later review and change it. The only possible exception seems to us to be that where a System policy has been adopted, the Board under the general provisions of the Act giving them broad supervisory powers, might require a change of rate after an appropriate interval to avoid a possible emergency and only after it became clear that such change wasnot only justified in the ordinary sense but that it was actually required in order to give effect to a necessary system policy. The assumption of the right by the Federal Reserve Board, as recently attempted, to initiate a change of rate, would appear to be predicated upon the theory that the right of "review and determination" is a continuous right of review, that once the directors of the Federal reserve bank had established a new rate which the Board had approvoed, they nevertheless have the right at any time to make a review of that rate and if not then found satisfactory, to establish a new one. The language of the present Act is so inept in expressing any intention to give the Board this continuous right of review (which could have been simply and effectively expressed by the use of other words) that we cannot believe Congress had any such intention.

Furthermore, we believe our view is upported by reference to Section 11 in which are enumerated the powers of the Federal Reserve Board and which reads in part as follows: "The Federal Reserve Board shall be authorized and empowered * * * (b) to permit or, on the affirmative vote of at least five members of the Reserve Board, to require Federal reserve banks to rediscount the discounted paper of other Federal reserve banks at rates of interest to be fixed by the Federal Reserve Board." At the time the Act was passed the Board consisted of seven members, and this provision required five votes out of seven to give the Board power to require such rediscounts and to fix the rate. Transactions of that character are infrequent and of comparatively minor consequence, while, on the other hand, probably most important act performed by a Reserve bank is a change of its established discount rate. It would seem inconsistent with the intention of Congress that fife out of seven votes would beqrequired to permit the Board to fix the relatively unimportant rate and at the same time enable the Federal Reserve Board to initiate a change of the established discount rate with only a majority vote.

Sixth. At the present time the Board's procedure is frequently embarrassed by the fact that it consists of eight members, and the possibility of a tie vote not only makes the decision of important questions of policy at times difficult or impossible, but also leads to the unsatisfactory possibility that the Board's position must sometimes be determined by whether the proposed action is in an affirmative or negative resolution; in other words, whether it is an attempt to adopt a new proposal which requires at least five votes with all in attendance, or whether it is an attempt to reverse a former action where four votes would have the affirmative effect of continuing action formerly taken.

It has seemed to me that the solution of this difficulty, if anamendment to the Federal Reserve Act should become necessary, would be to require either that the governor of the Board should be given two votes or that at least five affirmative votes should be required in order to enable the Board to initiate a change of rate.

Seventh. After thirteen years discussion of this matter which has been recurrent since January of 1915, I am personally of the opinion that, with suitable safeguards, the Board should have the power in an emergency or when a System policy so requires and some individual bank is recalcitrant, to initiate a change of rate. But even in such a case it should be provided that the number of votes required should be large enough to insure that hasty and ill-considered action is not possible.

If the Federal Reserve Board would agree upon a formula which would be satisfactory to all parties interested it should be designed to obviate this difficulty. I should hope that by that method all need for a resort to the courts or an amendment by Congress could be obviated.

I am inspired to write this letter because of the number of letters which are now coming to me from officers of other Federal reserve banks, indicating their desire to have the matter settled without further controversy and agitation.

I beg to remain,

Respectfully yours,

Hon. A. W. Mellon
Secretary of the Treasury,
Washington, D. C.

BS/RAR

Spare copy

PRIVATE AND CONFIDENTIAL: SEPTEMBER 21, 1927.

My dear Mr. Governor:

Word reaches me that considerable notice has been taken in the press abroad of what may appear to be a serious controversy between the Federal Reserve Board and the Federal Reserve Bank of Chicago in regard to the recent reduction of discount rate, and I think I should write you explaining something of the circumstances.

The language of the Federal Reserve Act on this point is as follows:

> Section 14.
> "Every Federal reserve bank shall have power **************
> (d) to establish from time to time, subject to review and determination of the Federal Reserve Board, rates of discount to be charged by the Federal reserve bank for each class of paper, which shall be fixed with a view of accommodating commerce and business."

It is difficult of exact construction and has been a disputed point ever since the Federal Reserve System was established. I shall not elaborate the various views as to the meaning of the Section. They are too many and varied to be recounted. In the present instance a policy was proposed at a meeting held in July, and with fair unanimity was adopted by those present in the hope that it would guide the whole System. The directors of the Federal Reserve Bank of Chicago did not necessarily disapprove of the policy as to other Federal reserve banks, especially New York, but rather held that the local situation within their district gave no indication of the need for a reduction. After a delay of a few weeks the Federal Reserve Board undertook to reduce the rate at Chicago from 4 to 3-1/2 per cent. The reduction was accepted by the directors and given immediate effect, and as San Francisco and Minneapolis promptly followed by similar reductions the whole System now has a 3-1/2 per cent rate of discount. In the meantime, however, it has been reported that the Chicago Federal reserve bank objected to the action of the Board; and the Federal Advisory Council has taken the same position; but the latter has expressed no view as to the wisdom of the policy of reductions of discount rates. They merely disapproved the method adopted by the Board.

Much unfortunate and misleading publicity has been given to the matter, and there has been considerable surmise as to whether the Chicago bank will test the powers of the Federal Reserve Board in the courts or whether Congress will be asked to clarify the Act by amendment. I hope that neither course will be necessary, but have no means of knowing what will eventually happen.

The significance of the incident can be much exaggerated. For thirteen years the Federal Reserve System has escaped a serious controversy on this point, and I hope that it can continue to do so without litigation or amendment to the Act.

Governor Crissinger's resignation, announced recently, had no relation to this development. He had informed me over a month before of his intention to resign which he could not do finally without awaiting the return of the President and Secretary Mellon; but his engagements already made were such that he could not defer carrying out his decision even though it did happen to come at an unfortunate moment.

The apprehensions expressed in some of the newspapers that this will result in a serious controversy throughout the country, I believe are exaggerated. There may be some discussion when Congress convenes which I hope will be minimized and result in no material changes in the Federal Reserve Act. Nor do I feel that there are likely to be any substantial changes in the policies of the System, - which in general have enjoyed increasing public approval and support.

Sincerely yours,

Monsieur Emile Moreau,
The Bank of France,
Paris, France.