THE HUMAN SIDE OF CENTRAL BANKING.

Address delivered to the

ORDER OF ARTUS

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Karl R. Bopp

Dean Phillips, Professors McManus and Nelson have stated clearly the importance of the Federal Reserve system in the lives of all of us:

> For the role played by the Federal Reserve System is at the heart of the explanation of the boom, as well as of the duration of the ensuing slump, and the policies of the Board as expressed in the System's operation are intimately connected with that explanation. (1)

> It follows, then, that the height of the recent boom and the depth of the depression are fundamentally the outcome of Federal Reserve credit expansion. The recent cycle may therefore properly be designated as a central banking phenomenon. (2)

How do mistakes of such magnitude occur? I believe a key can be found in a study of the men in charge of the system during this period. When we speak of the Federal Reserve system, we are speaking of more than 125 major officials. Federal Reserve policy is determined by a balance

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1. C. A. Phillips, T.F. McManus, R.W. Nelson, Banking Policy and the Business Cycle, New York, 1937, p. 117.

2. Ibid., p. 140.

of power within and among three sets of officials: first, a Baard composed of "...actual, living men, sitting ... in the shadow of the United States Capitol,"[3] second, the Federal Reserve Bank of New York controlled by "... men who come to the front in New York as bankers ... (and who), so to speak, belong to the master class in banking ... usually (able to) put their ideas over upon those of less prestige and experience,"[4] and third, the other eleven Reserve banks whose officials are these men of less prestige and experience.

Such is the highly complicated, yet human organization known as the Federal Reserve system. Mr. A. C. Miller of the Board recognized that they act like human beings when he stated:

> I should say ... that action by the Federal Reserve Board usually lies midway between a deliberate or calculated action, such as is taken with full appreciation of the consequences, and what you may call unconscious

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3. 70th. Congress, 1st. session, Hearings on H. R. 11,806, Washington, 1929, p. 184.
4. Ibid., p. 127

action. (5)

When the reserve system was established, apparently most of the officials were interested in cooperatively making a success of the undertaking. Neither the Board nor the banks wished to assume the initiative in determining policy. The banks asked the Board for suggestions as to rates, and the Board permitted the banks a large degree of freedom as to rates.

The recent Nye-Clark investigations of the Munitions' Industry, however, show that conflicts soon developed. Two leading figures in this early period came from rival financial groups in New York. Paul M. Warburg, of the Board, had been a partner in Kuhn, Loeb & Co. and was sympathetic to Germany, the land of his birth. Benjamin Strong had been President of the Bankers Trust Co., organized by H. P. Davison of J. P. Morgan & Co. Both Strong and the Morgan firm were strongly pro-ally from the beginning.

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5. 69th. Congress, 1st. session, Hearings on H.R. 7895, Washington, 1927, p. 647.

As early as November 10, 1916, Mr. Warburg wrote a letter to Strong stating:

> If the developmentx of the Federal Reserve System is not to lead to a more ruthless cracking of the whip on the part of the Board, or an increase of its functions and powers ... I think the boards of directors of the Federal Reserve banks must realize that readier cooperation with the Board is their duty and that they should stop fussing with policies and the interpretation of legislation and attend to the routine business upon a common plan and upon common principles. (6)

On November 16, 1916, Mr. Davison interviewed President Wilson regarding a proposed flotation by Morgans of British Treasury bills and notes. On the next day Davison had a meeting with the Federal Reserve Board in which he acted in a high-handed manner. Consequently, on November 29, the Board, after consultation with Wilson, issued a strong warning to the banks and public against purchase of foreign government securities. The warning ruined the market for the notes, and the proposed issue was abandoned. Secretary McAdoo returned to Washington, deeply incensed at the warning of the Board.
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6. 74th. Congress, 2nd. session, Hearings on S. Res. 206 of the 73rd. Congress, Washington, 1937, p. 9958.

On December 26, Governor Harding, at the instigation of McAdoo and without prior consultation with the other members of the Board, announced publicly that the Federal Reserve Bank of New York had been authorized to appoint the Bank of England as its correspondent and agent. This announcement violated the agreement of secrecy between Governor Strong and the Bank of England. The reaction of the New York Bank officials may be gleaned from the following letters:

> Since I saw the Board's announcement of the B. of E. matter this morning I have been hitting every ceiling in sight, and have imagined you going entirely out of sight. Indeed, since I received no reply from you to my wire this a.m. I fear you may literally have gone out of sight. (7)

To which Strong replied:

> ... in all honesty I must say that a repetition of this business means that I am through with the Federal Reserve Bank forever. ...The possible explanations of their actions are ... 5th, that it was a means taken by the Board to exhibit the strong arm in the general direction of the affsirs of the Federal Reserve System and suppress somewhat the independent activities of the Federal Reserve Bank of New York and partic-

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7. Ibid., p. 9548 (Pierre Jay to Strong, December 26, 1916).

> ularly myself. (8)
> ...If the Board takes the attitude ... that the Board alone is to be the judge of the character and extent of the publicity, then it becomes essential for the protection of the management of the Reserve banks that the Board should not be advised of confidential transactions. (9)

I am not here interested in the technicalities of the conflict, but solely in demonstrating that ill-feeling existed between the Board and the New York Bank before we entered the War and that the New York Bank felt justified in not advising the Board of all matters.

When we entered the conflict all our resources - including those of the Federal Reserve system - were enlisted to prosecute it successfully. The Overman Act concentrated unusual powers in the President by providing that "For the national security and defense, for the successful prosecution of the war ... the President is hereby authorized to make such redistribution of functions among executive agencies as he may deem necessary, including any functions, duties and powers hitherto by law conferred upon any

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8. Ibid., p. 9550.
9. Ibid., p. 9552.

executive department, commission, bureau, agency, office, or officer ..." The members of the Board quite properly interpreted this to mean that any opposition on their part to the Treasury program would merely mean that Secretary McAdoo would have his father-in-law, the President, transfer their powers to the Treasury Department. In other words, the Board became an unnecessary cog in the machine of government finance. Its sole deliberative function became rubber-stamping the Treasury Policy. The prestige of the Board was at low ebb during the war. But the Board was composed of active men. With their real reason for existence gone, the members became active in other ways. They wrote letters to each other and became concerned about the minutiae of operations. C. S. Hamlin kept a diary and prepared an index-digest of the Federal Reserve Bulletin.

McAdoo found it much more convenient to deal directly with the Reserve banks, especially with Governor Strong of the New York Bank. Thus the prestige of Strong rose as that of the Board declined. Strong was the man who - with the

Secretary - developed policy; the Board had no need for policy.

It was the New York Bank, therefore, which was prepared and in position to take the leadership when the operations of the Treasury ceased to be the dominant element in the banking situation. On April 10, 1920, Mr. Miller addressed the governors of the Reserve banks as follows:

> ... By this I mean to indicate that more and more the responsibility is getting to be concentrated upon the Federal Reserve banks, and within the Federal Reserve banks, upon you men who govern. For the first time, as I see it, you are in a situation where you are going to be given an opportunity to demonstrate whether, wisely or unwisely, you were invested with the title and the power and the responsibility of being governors.
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> ...So that I, for one, as a member of the Federal Reserve Board ... shall look to what the governors of the twelve Federal Reserve banks do as the main factor of efficiency in the policy of credit control which we can announce to be the Federal Reserve policy for the future and by which we are prepared to stand or fall. (10)

How well did the governors discharge this responsibility? which was placed upon them by the Federal Reserve Board? Again, Mr. Miller

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10. Mimeographed Report, p. 520 ff. In the library of the Federal Reserve Board.

testifies:

> As I look back upon the period following closely upon the termination of the war, for about three years, the banking system of this country ... was a good deal like a ship at sea without adequate equipment of rudder and compass to guide it. (11)

Storms soon beset the rudderless system. On May 17, 1920, the Senate adopted the Resolution introduced by Senator McCormick of Illinois which

> Resolved, that the Federal Reserve Board be directed to advise the Senate what steps it purposes to take or to recommend to the member banks of the Federal reserve system to meet the existing inflation of currency and credits, and consequently high prices; and what steps it purposes to take or recommend to mobilize credits in order to save the 1920 crop.

The Board attempted to avoid this rock of Scylla by a deflationary policy inaugerated at the famous deflation Conference with the Federal Advisory Council and the Class A directors of the Reserve banks, held on May 18, 1920.[12] Again Mr. Miller testifies:

> I think one of the chief troubles with the

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11. 69th. Congress, 1st. session, Hearings on HR. 7895, Washington, 1927, p. 696.
12. 67th. Congress, 4th. session, Senate Document No. 310, Washington, 1923,

> Federal Reserve system in 1920 was hysteria - hysteria in part due to the interefrence of Congress through a Senate resolution, with the maintenance of a well-balanced frame of mind in the Federal Reserve system. (13)

The Board soon found the good ship Federal Reserve in the whirlpool of Charybdis when Congress appointed the Joint Commission of Agricultural Inquiry whose report blamed the severity of the depression of 1920-1921 upon the improper policy of the Reserve system.

Since the Board was blamed for the results of Reserve policy, it began to assume greater initiative in that policy. But what policy should it adopt? It is perhaps more than a coincidence that during the period 1923-1930 - the period which has been most severely criticized - only one regular member at a time was <u>even nominally</u> a banker. The first of these was the nominal banker, Daniel R. Crissinger, one of the group from Marion, Ohio, whom President Harding brought to Washington to round out the Ohio gang. Crissinger was the only banker member among the regular members from May, 1923, until September,

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13. 70th. Congress, 1st. session, <u>Hearings on H.R. 11,806</u>, Washington, 1929, p. 163.

1927. He was succeeded by Roy A. Young as the only banker from October 1927, to September, 1930.

The newly energized but amateur Board adopted the policy recommended by the Secretary of the Treasury, who had been coached by Governor Strong. The Board began to force its policy - that is to say, the Strong policy - upon the outlying Reserve banks. That was the balanee of power in 1927. Two instruments were used to ease the money market. First, the Open-Market Investment Committee purchased large amounts of government securities in the open-market. In the second half of 1927. Mr. Miller later said of these purchases:

> That was under Federal Reserve bank leadership. I make it specific. It was an operation that was initiated, proposed, and developed by the Federal Reserve Bank of New York, accepted by most of the other banks Reserve banks who participated in the discussions, and, I regret to say, by the Federal Reserve Board. (14)
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> Coupled with the heavy purchases of acceptances it was the greatest and boldest operation ever undertaken by the Federal reserve system, and, in my judgement, resulted in one of the most costly errors committed by it or any other banking system in the last

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14. 74th. Congress, 1st. session, Hearings on S. 1715 and H.R. 7617, (Senate), Washington, 1935, p. 689.

75 years. (15)

The second instrument was reductions in rates of rediscount. On July 29, 1927, the Federal Reserve Bank of Kansas City reduced its rate from 4% to 3½%. The Boston and New York Banks followed within a week, and other Reserve banks soon fell into line. On September 2, the directors of the Chicago Bank voted not to reduce their rate. The Federal Reserve Board, informed by telegram of this action, split into two factions. Cunningham and McIntosh of the Chicago district, James of the St. Louis district, and Crissinger of the Cleveland district were indignant and promptly voted not to approve the decision of the Chicago Bank. Hamlin and Platt dissented strongly. Governor Crissinger notified the Bank that it would be permitted to continue the 4% rate only until Tuesday, September 6. On that day Mr. Miller arrived in Washington and aligned himself with the dissenters. On the same day Secretary Mellon, just returned from Europe, heard of the situation at the New York Bank. He informed Gover-

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15. 71st. Congress, 1st. session, Hearings on S. Res. 71, Washington, 1931, p. 134.

nor Crissinger that he disapproved forcing the Chicago Bank into line and requested that the Board's decision be delayed until he reached Washington. On the same day the Chicago Bank notified Crissinger that a quorum of the directors could not be secured until Friday.

"Between the pointed comment of some of the minority on this occasion, the 'obstinacy' of the Chicago directors, and the 'interefrence' of Secretary Mellon, Governor Crissinger's jealousy of his authority and zeal to demonstrate it were now thoroughly aroused."[16] Had Crissinger awaited the arrival of Mellon, a motion to force the 3½% rate upon the Chicago Bank would have lost by a tie vote. Therefore, he called an immediate meeting, did not communicate Mellon's message, and by a four to three vote forced the Chicago Bank to decrease its rate. Nine directors of the Chicago Bank were opposed to the reduction; four members of the Board were opposed to forcing the change; yet

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16. J. M. Daiger, "Did the Federal Reserve Play Politics," In Current History, October, 1932, pp. 25-32. The above description is condensed from Daiger's article.

the four members who favored the motion won the battle; but they lost the campaign! In a few days President Coolidge returned from the Black Hills, and on September 15, Secretary Mellon (Sic!) confirmed a rumor that Governor Crissinger had resigned.

The strong arm policy of the Board led to much criticism. The Board was cowed into submission; and as Mr. Miller testified:

> As things then were, the Board looked for the initiation of further measures of restraint to the Federal Reserve banks and they, in turn, depended upon the leadership of the Federal Reserve Bank of New York. And New York's leadership proved to be unequal to the situation. (17)

Briefly, then, the situation late in 1928 may be summarized as follows: Governor Strong died on October 16, 1928. The Board concluded that the leadership of Governor Harrison (Strong's successor) was unequal to the situation. Yet it had to be careful in initiating policies because of the consequences to it of the Chicago rate case. The Board looked to new instruments. It began by requesting on October 5, 1928, all Reserve banks to give reasons for any suggested

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17. Congressional Record, July 26, 1935, p. 12,405.

rate changes. All Reserve banks complied with this request, except the Federal Reserve Bank of New York.[18] On February 2, 1929, the Board sent a letter to Federal Reserve banks; and on February 7, it issued a warning designed to accomplish liquidation, presumably of the stock market. The New York Bank did not cooperate with the Board in the use of the new instruments of direct action and warnings.

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18. 71st. Congress, 3rd. session, Hearings on S. Res. 71, Washington, 1931, p. 172.

Between February 14 and May 23, 1929, the New York bank applied for an increase ten times; but not until April 9 did Governor Harrison send the Board an official statement of the reasons for the desired increase. However, both the governor and the chairman of the board of the New York bank reviewed the situation with the Federal Reserve Board on several occasions. Gov. Harrison stated (*Ibid.*, p. 84): "There was never a time, I think, when the Federal Reserve Board was not completely and wholly familiar with what reasons we had." Except for a particular reason on one occasion, by one member, the bank voted unanimously for the change, week after week (p. 84).

In May, Governor Harrison ceased his weekly demands for a 6% rate. Instead he apparently began a series of diplomatic negotiations. The argument which had been used by the opposition Board members, led by A. C. Miller, was that "legitimate" business should not be penalized with the higher rate. Harrison was finally successful when he agreed to reduce the buying rate on acceptances by ⅛% at the same time that the discount rate was increased to 6%. Apparently the division on the Board was Secretary Mellon, Governor Young, and Vice-Governor Platt for the bank and the remainder of the Board against the bank. (74th. Congress, 1st. session, Hearings on S. 1715 and H.R. 7617, (Senate), Washington, 1935, p. 955.

On February 14, 1929, the New York bank directors voted to increase the rate to 6 per cent. Governor Harrison, of the bank, telephoned the Board for approval (i. e., "review and determination") of the increase.[19] The Board decided that the proposal for an increase involved a national question which required study. Consequently they voted to take the application under review for consideration. When Governor Young, of the Board, advised governor Harrison of this decision, the latter answered that the directors of the New York bank had voted that the Board should decide the matter immediately; and that the directors could not leave until the issue had been decided. The Board viewed this imposition of an immediate decision as an unwarranted dictation of policy by the bank to the Board. As a result, the vote of the Board was unanimous against the increase. According to C. S. Hamlin, a member, the vote was unanimous *because* some of the members *who favored the rate change* refused to accept the imposition of the condition by the bank.[20] Hamlin's statement implies that the Board was divided in its opinion of the wisdom of the rate increase *per se*.

On February 15, 1929, the Federal Advisory Council passed a resolution which backed up the position of the board. The resolution, in part, read:

> The Council believes that every effort should be made to correct the present situation in the speculative markets before resorting to an advance in rates. (21)

Two years later some members of the Board rejoiced in this approval of the Council. These members did not state, however, that the Council shortly began to change its position. On April 19 it recommended:

> Measures so far adopted have not been effective. . . . The Council, therefore, recommends that the Federal Reserve Board permit the Federal Reserve banks to raise their rediscount rates immediately and maintain a rate consistent with the cost of commercial credit. (23)

Within another month the Council had reversed its original position entirely and favored the banks. Part of its recommendation of May 21 follows:

> The policy pursued by the Federal Reserve Board has had a beneficial effect, due largely to the loyal cooperation of the banks of the country. The efforts in this direction should be continued. The council notes, however, that while the total amount of reserve credit used has been reduced "the amount of the country's credit absorbed in speculative security loans" has not been substantially lowered.
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> Therefore, the council recommends to the Federal Reserve Board that it now grant permision to raise the rediscount rates to 6 per cent to those Federal Reserve banks requesting it . . . thus best safeguarding commerce, industry, and agriculture.(24)

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19. 71st. Congress, 3rd. session, Hearings on S. Res. 71, Washington, 1931, pp. 142-143.

20. Ibid., p. 172. Testimony of Mr. Hamlin: "On that first application, the Board was unanimous in rejecting it. I want to add in fairness to my associates that some who favored the application for increase, agreed that the condition imposed of an immediate decision could not be accepted by the Board, and therefore joined in a unanimous rejection of the application." Vice-Governor Platt was in favor of increasing the rate to 6 per cent in February, 1929; p. 215.

20-24. Sixteenth Annual Report of the Federal Reserve Board, Washington, 1930, p. 218.

These occurrences show the position of the Council in the working Reserve system. Although it was designed originally as an integral part of policy determination, from the beginning it has been unimportant but serves well for back-shifting when occasion arises.

Since the Board was in control, and since most persons expected it to stop at nothing to break the stock market, the speculative community watched its every move. In March of 1929 it held protracted daily sessions. On March 23 it held a Saturday session—a day which is usually *dies non.* The Board also shrouded its meetings in great mystery. "No statement" was the reply to inquiring reporters. The speculative community became hysterical, and severe declines in the market occurred on March 25-26, when a large Chicago bank decided to cooperate with the Board by calling $50.000.000 of loans in the Chicago market. The pressure spread at once to New York. This panic was stemmed by a member of the board of directors of the New York bank in defiance of the Federal Reserve Board. Mr. Mitchell, head of the National City Bank, placed $25,000,000 at the command of the call market. To provide against a repetition of the Tuesday jump in the call rate from 12% to 20% he let it be known that his bank stood ready to lend that much more in the call loan market. It would lend $5,000,000 at 16%, another $5,000,000 at 17%, and a like amount for each succeeding rise of 1% up to 20.[25]

The New York *Herald Tribune* on March 27, quoted Mr. Mitchell, as having said:[26]

> So far as this institution is concerned we feel that we have an obligation, which is paramount to any Federal Reserve warning, or anything else, to avert, so far as lies within our power, any dangerous crisis in the money market. While we are averse to resorting to rediscounting, for the purpose of making a profit in the call market, we certainly would not stand by and see a situation arise where money became impossible to secure at any price. (26)

Although the National City Bank frequently borrowed in larger volume and for longer periods, it is significant that its borrowings from the Reserve Bank increased to $25,000,000 on March 25, and to $35,000,000 on the 27th. On the 28th, the borrowings were back to zero.[27] The Action of Mr. Mitchell was regarded as open defiance of the Board. Within a few days the National City Bank issued a special bulletin which stated in part:[28]

> [The] Bank fully recognizes the dangers of over-speculation and endorses the desire of the Federal Reserve authorities to restrain excessive credit expansion for this purpose. At the same time, the bank, business generally, and, it may be assumed, the Federal Reserve banks, whose policies over the past year have been marked by moderation, wish to avoid a general collapse of the securities market such as would have a disastrous effect on business. (28)

25. Commercial & Financial Chronicle, March 30, 1929, p. 1968.
26. Reprinted, Ibid., p. 1968.
27. 71st. Congress, 3rd. session, Hearings on S. Res. 71, Washington, 1931, facing p. 322.
28. R. B. Westerfield, "The Current American Controversy Concerning Central Bank Policy," Torino, 1931, p. 74.
29. 71st. Congress, 3rd. session, Hearings on S. Res. 71, Washington, 1931, p. 175.

The New York bank was not alone in its disagreement with the Board concerning rates in 1929.[30] Although apparently some of the Reserve banks in the agricultural areas agreed with the Board on the use of instruments,[30] some of the larger Reserve banks desired rate increases. As early as March 15, 1929, the Chicago Bank made efforts to secure the approval of the Federal Reserve Board to an increase in rates. On March 28, the Board voted unanimously that the rate is the most effective instrument to protect credit against misuse. Several additional requests for a rate increase were made to the Federal Reserve Board before May 31, but the Board did not concur.[31] Similarly, the board of the Philadelphia bank voted to raise its rate on March 26, 1929; but the change was not approved by the Federal Reserve Board. On April 3, the resolution was repeated. This application expired by limitation on April 6 because of the failure of the Board to approve it. Again, at every meeting of the directors of the Boston bank and at one executive committee meeting between March 27 and June 5 votes were passed to raise the rate from 5 to 6 per cent. In each case the vote of the bank directors was unanimous. When the Board failed to approve these votes, the directors of the Boston bank rescinded them.[32]

30. B.H. Beckhart, "Grundsätzliches zur amerikanischen Notenbankpolitik." In Mitteilungen des Verbandes österreichischer Banken und Bankiers, Vienna, XIV, pp. 267 ff.
31. 71st. Congress, 3rd. session, Hearings on S. Res. 71, Washington, 1931, p. 756.
32. Ibid., pp. 753-755.
33. 74th Congress, 1st. session, Hearings on S. 1715 and H.R. 7617, (Senate), Washington, 1935, p. 952.

By the beginning of 1930, therefore, both the Board and the New York Bank had had their innings. The outlying Reserve banks desired an opportunity to influence policy. Evidence of this is found in the reorganization of the old Open-Market Investment Committee. The 1927 committee which had embarked upon the extensive operations later subject to so much criticism, was not really a system committee but was dominated by Governor Strong. On March 25, 1930, the old committee was reorganized into the Open-Market Policy Conference, composed of representatives from all the Reserve banks. Resolutions were passed by the committee and had to be approved by the Board. The executive committee could act only upon the authorization of the full committee. This more complicated procedure slowed up open-market operations considerably. Later the Banking Act of 1933 ~~introduced~~ codified a similarly ~~an~~ elaborate system of checks and balances. The Federal Open-Market Committee, which initiated the policies, was not in position to ratify them; the Board which ratified the policies, was not in position to initiate them or to

insist that they be carried out. The several Reserve banks had power to nullify the policies after they had been initiated and ratified. Governor Harrison testified:

> The result of that is, and I admit it, that as long as we have an open market policy conference, which is composed of 12 different individuals from 12 different parts of the country, even though we get agreement as to policy, it sometimes takes time. The result, again, is that we sometimes have gone slower in our policy than some of the rest of us might like to go. The corollary to it is that, having embarked upon a program and the conditions that we desire to accomplish having been accomplished, and the necessity for going into reverse having arisen, we are sometimes too slow in going into reverse, and that, I am frank to say, is an unfortunate incident to a banking system which, however wisely conceived, must operate through 12 different reverse banks, subject to the approval of the Federal Reserve Board. (33)

An example of this occurred in August, 1931. The Board, in conference with the New York bank, decided that a major purchase of securities was absolutely necessary. The open-market committee were called together. Governor Meyer, of the Board, discussed the matter with the members and urged the purchase of, say, 300 millions of Government securities. The open-market committee voted 11-1 to reduce the 300 millions to some 100 millions. The strong opposition encountered from some of the Reserve banks resulted in a much smaller purchase of securities than had been contemplated.[34] The Board acquiesced in the limitation.

Similarly, Mr. Hamlin testified concerning operations under the new Act:

> In 1933 the matter came up again . . . I attended a meeting at the Federal Reserve Bank of New York of the executive committee. Governor Harrison reported that the Federal Reserve Banks of Boston and Chicago had passed resolutions absolutely declining to participate in any further open-market purchases unless in cases of grave emergencies, and the Governor at that time was very much worked up. He felt that we should go ahead strongly and vigorously, and pointed out that if New York did it alone—and New York, I think, was somewhat inclined to do it—it would pull its reserve ratio down to 47 per cent, leaving the reserve ratio of Chicago

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33. 72nd. Congress, 1st. session, Hearings on H.R. 10,517, Washington, 1932, p. 476.
34. 74th. Congress, 1st. session, Hearings on S. 1715 and H.R. 7617, (Senate), Washington, 1935, pp. 750,760, 945.

and Boston at 70 per cent. The Governor delivered an oration worthy of Demosthenes. He nearly drew tears to my eyes, when he told us that it was the duty of the Board to force Boston and Chicago into line. I agreed with him entirely. I said, "I don't know how we can do it, but I will go back and see what can be done."

Then he made a very interesting suggestion, that the Board might be able to do that if New York were to take practically this whole issue—the Board could require Boston and Chicago to rediscount for New York and thus equalize the reserve ratio. . . . .

Such was the status when Mr. Roosevelt assumed office and decided to concentrate control over the banking system in Washington. After a number of conferences with Mr. Eccles, the latter drafted Section II of the Banking Act of 1935 which was passed substantially unchanged by the House by a vote of 271-110.

I spent some time in Washington in the summer of 1936 trying to secure the background of this Act. In the 73rd. Congress the Senate Committee on Banking and Currency consisted of twelve Democrats and eight Republicans all grouped into ten sub-committees. Three Republicans: Goldsborough (Md.), Walcott(Conn.), and Kean (N.J.) were replaced by three Democrats: Maloney (Conn.), Radcliffe (Md.), and Cutting (N.M.).

Before the proposed Act reached the full committee for discussion , it was referred to

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35. Ibid., p. 948.

the sub-committee on Monetary Policy, Banking, and Deposit Insurance. Now, whereas the full committee was headed by Duncan U. Fletcher, a leader for the administration; this sub-committee was headed by Carter Glass, an out-spoken critic of the legislation. In addition to Glass, the sub-committee was composed of Bulkley and McAdoo, Democrats, luke-warm in favor of the whole bill as a compromise to secure deposit insurance; and Townsend, the only remaining Republican - Wolcott having been defeated for reelection. Senator Fletcher faced the possibility of defeat for the Act in the sub-committee before it even reached the whole committee. His job was to see the Act passed to give the administration control.

A number of possible solutions were proposed. First, Fletcher might appoint himself as chairman of the sub committee. The objection to this procedure was that it would violate Congressional etiquette and would be a direct slap in the face to Glass. Second, Fletcher might have appointed himself a regular member of the sub-committee. The trouble here was that Fletcher

would not serve under Glass. Consequently, he hit upon another scheme.

At an early meeting of the whole committee Fletcher noted that three members of the old committee had been defeated in the recent elections and had been replaced by three new members. Furthermore, the division of the whole committee into ten sub-committees was no longer wise because some of these sub-sommittees had completed their work. Therefore, Fletcher proposed a complete reorganization of the sub-committees. He could not remove members from sub-committees; but, in-as-much as the sub-committee on Monetary Policy was now so important, he greatly increased its size. In short, he packed it for the administration by increasing it from five to eight members. Since he had to retain the old members, the packing gave the administration three certain votes for the bill, four possible votes for, and two certain votes against.[36] In general, I was informed, the votes were five to four for

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36. For: Bankhead, Cutting, Norbeck,
Uncertain: Bulkley, Byrnes, Couzens, McAdoo
Against: Glass, Townsend.

the administration measure. Then, Bronson Cutting, one of the certain votes for, was killed. This reduced the typical vote to four for and four against! Again Fletcher was stumped. After careful consideration, the administration forces decided upon the following stratagem. Whenever a matter of little significance was raised, they would make the motion to pass and lose by a tie vote. But whenever a matter of major significance was raised, they permitted the Glass faction to make the motion - which would also lose by a tie vote!

So it happened that although Glass was able to introduce many changes in the Act, yet the administration was able to concentrate control of the Federal Reserve system in Washington.