

TOP SECRET

MEMORANDUM FOR The Secretary of the Treasury and
The Chairman of the Board of Governors
of The Federal Reserve System

During the past few months I have discussed with each of you many times my concern over the problem of inflation and the approaches which might be taken by the Government to control it. The Government has during this period taken many steps to bring the problem of inflation under control.

In my consideration of the inflation problem, I have been aware of the difficulties faced by the Federal Reserve System in controlling private credit expansion at a time when we have a large public debt. All of us recognize, of course, that credit expansion is simply one phase of the whole inflation problem; and that, in fact, some credit expansion is necessary to facilitate the growth of production which is essential to the defense effort. But, the expansion of loans, not only by the banking system but by financial institutions of all types, adds fuel to other inflationary forces and must be stopped to the greatest extent possible consistent with the needs of the defense effort. In stopping credit expansion, however, I feel that we should use measures that are fully consistent with maintaining stability in the Government security market and confidence in the credit of the United States.

As you know, it is likely that we shall have to borrow billions of dollars to finance the defense effort during the second half of this calendar year because of the seasonal nature of tax receipts which concentrate collections in the first half of the year and the inevitable lag between the imposition of new taxes and their collection by the Treasury. It is my hope that such new money as it is necessary for the Treasury to borrow during the months ahead to finance our military requirements can be obtained in the least inflationary manner possible, that is, from true investors outside of the banking system.

With these considerations in mind, I ask that each of you give thought to the type of program that might be worked out along the following lines -- a program which would provide the necessary restraint on credit expansion and at the same time make it possible to maintain stability in the market for Government securities. This program would . . . (1) control bank loans through the utilization of the powers provided by the Emergency Banking Act of 1933 and, possibly, the Trading with the Enemy Act; (2) set up a committee similar to the Capital Issues Committee of World War I; and (3) further restrain the lending and mortgage insurance activities of the various Government credit agencies.

It is my belief that the addition of the foregoing to the present selective credit controls will provide a well-balanced program of credit

-2-

curtailment. It will do the very thing that each of us has been so concerned about in recent months -- that is, effectively restrain the expansion of loans. Pending the development of this program, I hope that no further attempt will be made to change the interest rate pattern, and that unquestioned stability in the Government security market, which is imperative at this critical time for the financing of the defense effort, will be maintained.