A meeting of the Board of Governors of the Federal Reserve System with the Federal Open Market Committee was held in Washington on Wednesday, December 18, 1935, at 12:45 p. m.

PRESENT: Mr. Eccles, Chairman
Mr. Thomas, Vice Chairman
Mr. Hamlin
Mr. Miller
Mr. James
Mr. Szymczak

Mr. Morrill, Secretary
Mr. Bethea, Assistant Secretary
Mr. Carpenter, Assistant Secretary
Mr. Clayton, Assistant to the Chairman
Mr. Thurston, Special Assistant to the Chairman
Mr. Goldenweiser, Director of the Division of Research and Statistics

Governors Young, Harrison, Norris, Fleming, Seay, Newton, Schaller, Martin, Geery, Hamilton, McKinney and Calkins, Members of the Federal Open Market Committee
Mr. Burgess, Secretary of the Federal Open Market Committee
Mr. Strater, Secretary of the Governors' Conference

Governor Harrison stated that the Federal Open Market Committee had been in session since yesterday morning and had discussed thoroughly the different aspects of the business and credit situation. He said that the Committee had considered the preliminary memorandum prepared by him under date of December 13, 1935, and a second memorandum on the subject of excess reserves, and that consideration was given at length to the statements of Messrs. Goldenweiser and Williams at the meeting yesterday. He added that as a result of the discussions a resolution had been adopted on eight affirmative and four negative votes, which contained a recommendation that the Board give consideration to an early increase in reserve requirements. At the request of Governor Harrison, Mr. Burgess read the recommendation for the information of the members of the Board.

Mr. Miller asked what was meant by an early increase in reserve requirements as used in the resolution and inquired what was in the minds of the members of the Federal Open Market Committee as to the criterion by which the Board should be governed in determining when action should be taken.

Governor Harrison stated that, while it had been felt that it was somewhat beyond the jurisdiction of the Committee to make a suggestion with regard to changing reserve requirements, it had been given to understand that the matter was an appropriate one for the Committee to express an opinion upon, especially in view of the submission to it of the recommendation of the Federal Advisory Council. He said that it was thought by the Committee that it would be difficult for it to suggest the date for action without knowing how much the Board would increase reserve requirements or to what classes of banks the increase would apply, and that if the Committee had suggested a date for action it would have been necessary for it to propose a complete program which it was not thought necessary or appropriate for it to do.

Mr. Miller stated that the resolution adopted by the Committee might lend itself to the interpretation that the Committee expected an early condition of economic recovery and that such a situation might be the element that would fix the early date. Governor Harrison stated such an interpretation was not intended.

Mr. Miller stated that, inasmuch as the Committee had recommended that action be taken at an early date, he would like to have an expression of opinion as to what early date was intended; that he felt that unless the members of the Committee were prepared to say what they would do if the responsibility for action were placed on them, they had not thought the problem through; and that he was left in doubt as to whether the resolution contemplated action in one month or in two months or whether the Board should be governed by some condition that was still in motion.

Governor Harrison stated that, while undoubtedly the members of the Committee had their individual opinions as to the time when action should be taken, the Committee as such had not undertaken to fix the date because it was felt that in order to do so it would be necessary to determine upon an entire program, and that it was thought that would be going too far in making a suggestion or recommendation to the Board.

Chairman Eccles stated that he interpreted the resolution as meaning that there was no urgent necessity for immediate action or indication of an emergency, but that, in view of the existence of the large volume of excess reserves, it was felt by the Committee that action should be taken at an early date before there was an expansion of bank credit, and that the Committee did not wish to relate the action of increasing reserve requirements to an expansion of bank credit but rather to the abnormal gold imports. He pointed out that the provision of law authorizing the Board to make changes in reserve requirements was given in order to enable the Board to prevent injurious credit expansion or contraction, and he raised the question whether the Board had authority to increase reserve requirements because of gold imports when there was no evidence of undue credit expansion. He also stated that if the Board should take action to increase reserve requirements when there was no such evidence of credit expansion it might be interpreted by the press and the public as a move to restrict credit, and that this interpretation would have an effect exactly opposite to that sought by an increase in reserve requirements.

Chairman Eccles then read excerpts from a letter which appeared today in the New York Times from Mr. S. Parker Gilbert which contained a discussion of the problem. Statements in the letter were discussed and Governor Harrison said that he felt the only risk involved from an adjustment in reserve requirements at this time would be that it might be misconstrued by the public as a change in the present easy money policy, and that undoubtedly a statement could be made that would offset to some extent or entirely that possible reaction.

Chairman Eccles expressed the opinion that there is a strong likelihood that the newspapers would misinterpret the action and that the banks would use it as an occasion for increases in interest rates.

Governor Harrison suggested that even if there were a slight increase in short term money rates, that would not be restrictive.

Mr. Miller stated that there had been almost no change in the situation since the last meeting of the Federal Open Market Committee and he inquired whether it was the opinion of the Committee that the country has suffered through the failure to increase reserve requirements.

Governor Harrison referred to the important factors of the continued unprecedented inflow of gold and the uncertainty as to how long the movement would continue, and stated that, while part of the movement might be the result of fear as to the situation abroad, it was believed also that the impression prevailed abroad that there would be a substantial inflation in the United States as the result of the huge volume of excess reserves which the monetary authorities would not or could not control.

Mr. Miller expressed the opinion that the resolution adopted by the Committee virtually admitted that those who fear inflation in the United States are right, and that the report was inflationary and one that lacked confidence that when intervention was justified on a broad scale it would be taken. He added that he felt that if the members of the Federal Open Market Committee had power to act in the matter they would not act as suggested in the resolution, and that the thought in the back of the minds of the members of the Committee was a vague distrust of the competency of the Board to act at the proper time.

Mr. Hamlin suggested that an increase in reserve requirements is a corollary to an increase in discount rates, in that a major increase in reserve requirements could be used in connection with the policy of restricting credit and a discount rate increase could be used to increase the cost of credit. Governor Harrison said that an increase in discount rates, when member banks were not borrowing, would indicate a desire for higher rates whereas reserve requirements could be raised at this time without affecting interest rates.

In response to Mr. Miller's statement, Governor Harrison said that he felt that what was in the minds of those who favored the resolution of the Committee was that it was believed that with excess reserves at the present large figure, and contemplating that action would be necessary at some time to reduce the excess reserves, it would be much less hurtful and damaging to the country to absorb a portion of the excess reserves, before they were used by the banks as a basis for credit, than to wait until such use was made of the reserves, when an increase in reserve requirements might result in deflation.

Mr. Miller said that, with the amount of excess reserves as large as at present, there was always the possibility of making a major adjustment in reserve requirements which would leave the bank situation in an extremely comfortable position. He then expressed the opinion that the longer action is postponed by the System, provided its judgment is correct as to when action should be taken, the stronger its position would be with the public. He also stated that he felt that the construction that would be put upon action at this time would be that it was action resulting from timidity.

Governor Young reviewed briefly the actions taken by the Federal

Open Market Committee at its separate meeting, prior to its action on the resolution referred to above, and stated that the intimation had come to the Committee that such a resolution would be welcomed by the Board, and that, if such was not the case, he felt the matter should be considered by the Committee and the Board with a view to reaching a satisfactory solution of the problem.

Chairman Eccles stated that he believed that the resolution in the form adopted by the Committee was the proper one as it did not suggest that immediate action be taken, but left the Board free to take the recommended action at any time in the near future that may seem to be desirable. He pointed out that should the resolution suggest the amount by which reserve requirements should be raised and that action be taken immediately, it would indicate the existence of an emergency which does not exist. He then pointed out that within the course of the next thirty days there will be further developments in connection with the budget for the fiscal year 1937, the bonus question, and other issues which have a relation to monetary policies and that these things should be taken into consideration in determining when action should be taken. He added that, if undue activity appeared in the securities markets, that development could be dealt with by the use of the powers given to the Board by the Banking Act of 1933 and the Securities Exchange Act of 1934. There were very few banks, Chairman Eccles said, that did not have excess reserves at the present time, whereas if action raising reserve requirements were deferred until further expansion was under way, and then reserves were increased to check undue expansion, it would result in a situation which would force a large number of banks to borrow from the Federal Reserve System or to liquidate assets, which would be decidedly deflationary in effect.

He also stated that it was estimated that because of the increased demand for currency over the Christmas holidays and increases in Treasury balances at the Federal reserve banks, excess reserves of member banks would be reduced to approximately $2,600,000,000 this week; that, in the absence of action by the System, they would increase to approximately $3,350,000,000 by the end of January, or a fluctuation of approximately 25%; and that the suggestion had been made that the Board of Governors of the Federal Reserve System might issue a statement to the effect that excess reserves of $2,600,000,000 were much larger than could be utilized by any healthy credit expansion, that there was no occasion for permitting excess reserves to increase beyond that amount, and that the Board would take such action as might be necessary to absorb any further increases in excess reserves. He added that such a policy could be made effective to an increased extent by the cooperation of the Treasury Department in drawing down Treasury balances in banks which have large amounts of excess reserves and keeping them on deposit with the Federal reserve banks.

Chairman Eccles then stated that, with no further increases of gold imports or purchases of silver during the coming year, there was a possibility of excess reserves increasing to approximately $3,300,000,000 by the end of January and, taking all possibilities into consideration, to as much as $4,000,000,000 before the end of the year, and that it was felt that, if action should be delayed until an increase in reserve requirements in a very large amount was necessary to reduce the excess to a reasonable figure, such action would be decidedly deflationary; whereas, if action were taken, while the excess reserves are at the lower level of $2,600,000,000, to prevent their increasing above that level, more drastic action would not be necessary. He pointed out, however, that if the latter policy were adopted it would be necessary for the Board to take action in the near future to prevent the increases in excess reserves which will occur after the end of the year.

Mr. Miller expressed the opinion that such action would announce a level above which excess reserves would not be permitted to go and would establish a very dangerous precedent.

Governor Seay stated that during the deliberations of the Federal Open Market Committee consideration had been given to the changes in the situation which would take place between now and the middle of January and that there was some disposition on the part of certain members of the Committee to defer action until January when another meeting of the Committee would be held.

Mr. Miller suggested that the most desirable action that could be taken at this time would be the issuance of a statement upon the adjournment of this meeting which would indicate that the situation had been very carefully reviewed by the Committee and the Board, that they were in agreement, and that action would be taken at a time when in their judgment action was necessary. He added that he felt it would be highly undesirable for the impression to persist that there was a division in the counsel given to the Board with regard to the action to be taken and that it had been impossible to develop a common attitude toward the problem which had been before the Board and the System for some time.

Governor Harrison stated that he wished to report that the Federal Open Market Committee had voted unanimously to request the Chairman to call another meeting of the Committee about the middle of January.

Governor Calkins said he had not voted for the resolution adopted by the Committee for the reasons (1) that he felt that it was outside of the province of the Committee to advise the Board as to what it should do about reserve requirements and (2) that he was not in favor of that method at the present time. He added that, if the suggestion that action be taken at an early date were eliminated from the resolution, it would be much less objectionable.

Governor Young stated that he had not voted for the resolution and that if he alone had the power he would act now by selling securities from the System portfolio, and that he would be willing to take full responsibility for that action.

Mr. Miller said that he felt that, if the matter were carefully considered by the Federal Open Market Committee and the Board, a majority, if not all, of the members could reach a conclusion with respect to what should be done in the way of action or a press statement at the present time, and that the most important matter for decision was the question of the statement to be issued to the press. He was of the opinion that, if there could be presented to the public a statement that the System was in substantial accord as to the policy that should be pursued, it would have a wholesome effect.

Governor Harrison suggested that perhaps the best opportunity for the System to take action without the risk of misinterpretation of its action would be shortly after, or coincident with, the budget message to Congress. He expressed the opinion that the resolution adopted by the Federal Open Market Committee was a fair recognition of the problem before the Committee and the Board and avoided what he felt would be an impropriety and a mistake on the part of the Committee if it should recommend that reserve requirements be raised immediately and in a certain amount. He suggested that, if action could be taken at the time of the budget message, provided it could be taken without a change in the present monetary policy, it would be considered favorably and as a wise action on the part of the Administration and the Federal Reserve System.

Chairman Eccles expressed the opinion that the resolution adopted by the Committee was entirely satisfactory except for the suggestion that action be taken at an early date. Governor Calkins suggested that the word "early" be eliminated from the recommendation. This suggestion was discussed briefly, and it was pointed out that if the resolution were amended in this way the recommendation might mean that action should be taken immediately.

Mr. Miller said that if the resolution were amended to eliminate the suggestion that action be taken at an early date, the whole matter should be reconsidered by the Committee.

Governor Martin suggested that the Board should take definite action and that, in the present circumstances, no action would be definite action, particularly in view of the recommendation of the Federal Advisory Council. He said that, if a statement could be made that the Federal Open Market Committee and the Board were in agreement that no action should be taken at this time, it would be an announcement of definite policy, and when the Committee met in January it would be in a position to make a similar statement if conditions justified or take affirmative action in the light of changes in the existing situation.

Mr. James suggested that, in view of the importance of the decision to be made, he felt it was highly necessary that the meeting continue long enough to afford each member of the Committee and the Board an opportunity to express his views, and for a full discussion of the elements of the problem, following which an agreement could be reached as to the action that should be taken, and a statement should be issued to the press which would dispel the popular idea that there was a difference of opinion among the officials of the Federal Reserve System as to the course that should be pursued.

Chairman Eccles stated that whether further consideration was to be given to the resolution adopted by the Committee was a matter for decision by the Committee. He agreed that an opportunity should be afforded for all members of the Federal Open Market Committee and the Board to make such observations or suggestions as they desired and that the meeting should be continued as long as necessary for that purpose.

Governor Seay said that the only conclusions that he felt it was possible for the Federal Open Market Committee to reach were (1) to adhere to the resolution that it had adopted, or (2) to state that the Committee had reviewed the business and credit situation and saw no reason for recommending any definite action at this time and had adjourned to meet in January when the situation would be reviewed again.

Governor Harrison suggested that perhaps the most expeditious manner of meeting the situation would be for the Board to reach a decision as to the action it feels should be taken, following which the matter could be discussed further with the Committee.

Mr. Thomas inquired whether the Committee would be willing to take action to increase reserve requirements immediately and, if not, what new developments would have to enter into the picture before the Committee would be willing to act.

Governor Harrison stated that he felt that it would be preferable to wait until approximately the middle of January when reserve requirements could be increased to absorb increases in excess reserves as suggested by Chairman Eccles; the amount of the increase in reserve requirements to be determined in the light of the amount of Treasury balances, the return flow of currency, and the budget message.

Mr. Thomas then inquired how the Committee would know what the conditions would be in January, and Governor Harrison replied that the longer action was deferred the more definite would be the available information with regard to the factors involved.

Mr. Thomas then asked why action should not be taken at this time, and Governor Harrison stated that the factors involved would be more clearly defined in January, which would enable the Board to act on the basis of more definite information.

Mr. Miller inquired whether the Committee had given consideration to the possibility that March of the coming year might show that business had not maintained its present momentum, and he stated that if action should be taken now to increase reserve requirements and recovery was not sustained, the System would be blamed for impeding recovery.

Governor Harrison replied that such a danger was always present in the present situation, and Mr. Miller said he felt that action should be delayed until the Committee and the Board are able to get as many of the necessary elements in the picture as possible.

Chairman Eccles suggested that in view of the long time that the meeting had been in progres it might be advisable to adjourn and, if necessary, reconvene later.

Governor Harrison stated that the Committee had finished its deliberations and had submitted its report, but that, if the Board desired, the members of the Committee would be willing to discuss the matter further.

Mr. Szymczak suggested that a separate meeting of the Board be held for the purpose of reaching a decision as to the action it felt should be taken, following which the Board could meet again with the members of the Federal Open Market Committee.

This suggestion was agreed to, the meeting was adjourned at 2:30 p. m. and at 3:30 p. m. the appointive members of the Board (Messrs. Eccles, Thomas, Hamlin, Miller, James and Szymczak) met in the Chairman's office. Messrs. Morrill, Bethea, Carpenter, Clayton, Thurston and Goldenweiser of the Board's staff were also present.

Chairman Eccles stated that he believed it would be possible for the Board and the Federal Open Market Committee to agree on a statement for release to the press which would state (1) that the System was anxious to take no action that would retard the improvement in business, (2) that there was no evidence of an undue expansion of credit, (3) that there was an abnormal amount of excess reserves brought about by large imports of gold, (4) that there was no need for these reserves as a base for reasonable credit expansion, and (5) that the Federal Open Market Committee and the Board were watching the situation and had decided that nothing should be done at the present time, and that the meeting of the Federal Open Market Committee had adjourned to meet again in January.

Mr. Miller suggested that the alternatives before the Board were (1) to say that the Board and the Federal Open Market Committee were keeping in close touch with the situation and the Committee would meet in January, or (2) to announce that something was going to be done at the present time to absorb a portion of the excess reserves. He said that he preferred the former course and felt that it would accomplish all that could be accomplished by the second alternative and possibly more.

Mr. James inquired whether the Treasury had a definite policy with regard to drawing down Treasury balances in depository banks, and Chairman Eccles said that at the present time the Treasury had a formula under which balances were drawn down in a proportionate amount throughout the United States, and that it might be possible to get the Department to shift balances from banks which have large excess reserves into the Federal reserve banks where they could be maintained for thirty days until a decision could be reached by the Board with regard to a change in reserve requirements on the basis of changed conditions after the end of the year.

Mr. James expressed the opinion that if assurance could be given that such a procedure would be followed it would be a satisfactory arrangement.

A draft of a statement that had been prepared along the lines suggested by Chairman Eccles was read and Mr. Miller suggested that the statement might be read to the members of the Federal Open Market Committee and, if they were in general agreement therewith, a committee composed of members of the Board and members of the Federal Open Market Committee could be appointed to place the statement in satisfactory form for presentation to the joint meeting of the Committee and the Board. He stated that the three important elements which should be included in the statement were (1) that the Federal Reserve System was not unaware of the magnitude of the problem, (2) that it was not indifferent to the consequences of any action that it might take, and (3) that a decision not to take action was not a policy of drifting but, in the circumstances, was positive action.

Mr. Hamlin moved that the procedure suggested by Mr. Miller be followed.

Carried unanimously.

After some further discussion of the points that should be covered in the proposed statement to the press, the members of the Board and the members of its staff returned to the meeting with the members of the Federal Open Market Committee in the Board room.

Chairman Eccles read the draft of statement which had been considered by the Board and expressed the opinion that the issuance of such a statement at this time with the unanimous agreement of the Board and the Federal Open Market Committee would be very favorably received.

During the ensuing discussion of the statement some of the members of the Federal Open Market Committee stated that they were not in agreement with portions of the statement and suggestions were made for its revision.

Governor Schaller inquired whether the public statement would take the place of the resolution adopted by the Federal Open Market Committee. Chairman Eccles said that he thought that, if a public statement were agreed upon, the resolution would not be submitted to the Board; that if it should be decided finally to submit the resolution all the Board could do would be to make its own separate statement to the press; but that before reaching a decision on that matter an endeavor should be made to determine whether there was a position upon which the Committee and the Board could agree in view of the proposed meeting in January, so as to avoid, if possible, any evidence of disagreement between the Committee and the Board as to the action that should be taken. He added that he would prefer to make no public statement, but felt that, in view of the attention which has been given in the press and by the public to the meeting of the Federal Open Market Committee, the issuance of a statement was unavoidable.

The suggestion was made that Messrs. Eccles and Miller, as representatives of the Board, together with Messrs. Thurston, Goldenweiser and Morrill of the Board's staff, and Messrs. Harrison and Young, as representatives of the Federal Open Market Committee, be appointed a committee to draft a statement for submission to the joint meeting.

Governor Norris stated that, as he understood it, several of the members of the Federal Open Market Committee felt that action should be taken in the near future either to raise reserve requirements or to dispose of securities from the System portfolio; that the Board apparently was indisposed to do either of these things at the present time; and that, while possibly a majority of the members of the Committee would prefer to stand on its resolution, it was highly important, in view of existing circumstances, that the meeting consider the possibility of a statement on which there could be unanimous or at least a majority agreement. He added that the reason for any reluctance that he might have to adopt such a procedure would be that a large section of the public feels that, if the Board will not take action when the conditions make such action as innocuous as it possibly can be made, it will not take action when conditions make it necessary and when the effect of the action would be much more serious than at the present time.

Governor Schaller suggested that if action were delayed thirty days it might be too late to adopt the suggestion made by Chairman Eccles that action be taken to prevent the increase of excess reserves from the low point of approximately $2,600,000,000 which they are expected to reach during the current statement week.

Chairman Eccles suggested that it might be possible for the Treasury Department to maintain its balances with the Federal reserve banks and excess reserves be kept at a low figure until the end of January, prior to which time another meeting of the Committee could be held.

After some further discussion, the suggestion that a committee be appointed to draft a statement was agreed to, and the members of the committee withdrew from the meeting for the purpose of preparing a statement. The other members of the Board and its staff also withdrew and reentered the room upon the return of the members of the committee to the meeting.

At the request of Chairman Eccles, Mr. Thurston read the statement that had been prepared by the committee as follows:

"The Board of Governors of the Federal Reserve System and the Federal Open Market Committee have given extended consideration to the general business and credit situation and to the recommendation of the Federal Advisory Council and are of the opinion:

1. That continued improvement has been made in business and financial conditions but that the country is still short of a full recovery.
2. That the primary objective of the System at the present time is still to lend its efforts to a furtherance of recovery.
3. That there is at the present time no evidence of over-expansion of business activity or of the use of business credit.
4. That the present volume of member bank reserves, which have been greatly increased by imports of gold from abroad, continues to be excessive, far beyond the present or prospective requirements of credit for sound business expansion.

"Therefore, the special problem created by the continuing excess of reserves has had and will continue to have the unremitting study and attention of those charged with the responsibility for credit policy in order that appropriate action may be taken as soon as it appears to be in the public interest."

Governor Young moved that the statement be approved.

Governor Seay inquired whether it was proposed to give out any additional explanation or confine the information given to the public to the proposed statement. Chairman Eccles stated that no additional statement would be made.

Governor Young's motion was put by the chair and carried upon the unanimous vote of the members of the Board and the members of the Federal Open Market Committee, with the understanding that the statement would be released immediately to the press.

Chairman Eccles called attention to the fact that no reference was made in the statement to a meeting of the Federal Open Market Committee in January, and stated that it had been decided that such a reference would be an undesirable one as it would be an indication that no action would be taken until that meeting, whereas circumstances might arise which would make it desirable that some action be taken before that time.

Thereupon the meeting adjourned.

Chester Morrill
Secretary.

Approved:

M S Eccles
Chairman.