

A meeting of the Board of Governors of the Federal Reserve System with the Federal Advisory Council was held in the offices of the Board of Governors in Washington on Monday, May 14, 1945, at 10:30 a.m.

PRESENT: Mr. Eccles, Chairman  
Mr. Ransom, Vice Chairman  
Mr. Szymczak  
Mr. McKee  
Mr. Evans

Mr. Morrill, Secretary  
Mr. Carpenter, Assistant Secretary  
Mr. Hammond, Assistant Secretary  
Mr. Thurston, Assistant to the Chairman  
Mr. Goldenweiser, Economic Adviser,  
Division of Research and Statistics  
Mr. Smead, Director of the Division of  
Bank Operations  
Mr. Paulger, Director of the Division  
of Examinations  
Mr. Parry, Director of the Division of  
Security Loans  
Mr. Leonard, Director of the Division  
of Personnel Administration  
Mr. Thomas, Director of the Division of  
Research and Statistics  
Mr. Vest, General Attorney  
Mr. Wyatt, General Counsel

Messrs. Traphagen, Kurtz, McCoy, Berry, Brown, Gifford, Baird, Bradshaw, Winton, and Wallace, Members of the Federal Advisory Council from the Second, Third, Fourth, Sixth, Seventh, Eighth, Ninth, Tenth, Eleventh, and Twelfth Federal Reserve Districts, respectively

Messrs. Thomas P. Beal, President of the Second National Bank of Boston, Boston, Massachusetts, and Charles E. Rieman, President of the Western National Bank of Baltimore, Baltimore, Maryland, who attended as observers in place of Messrs. Spencer and Fleming, respectively

Mr. Lichtenstein, Secretary of the Federal Advisory Council

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Mr. Brown stated that the Board had asked for the views of the Council with respect to how the inflationary developments in farm and urban real estate and other capital assets should be dealt with, and he summarized the views of the Council on that point substantially as follows:

I think the Council was unanimous in its opinion that, now that the European phase of the war is ended, all possible pressure should be put on the armed forces to reduce military expenditures and to allow more civilian production both in goods and housing. I think all of us feel that the armed forces, if left to themselves, will keep an army and navy of maximum size and unless some pressure is put upon them they will keep an entirely unnecessary force of men. Mr. Robert E. Wood of Sears-Roebuck and Company has just returned from a flight around the world and says that there are already more tanks, airplanes, and jeeps than could possibly be used against the Japanese and that in his opinion there could be a reduction of at least \$36 billion a year in war expenditures without any harmful effect on the war against Japan. The Council does not believe that there is any way to meet the inflationary situation other than by the production of more civilian goods and housing.

I do not think the Council feels that speculation in stocks and real estate, either urban or farm, has reached a dangerous point. Farm lands are about where they were in 1913. Speculation in urban real estate is not in the form of speculation in small houses. The situation is such in most parts of the country that anyone who owns a house will not sell it and people will pay almost any price to get a house because they can not rent one. There has been a good deal of speculation in the larger apartment buildings and hotels and in some kinds of commercial buildings, but even there the prices are below the cost of reproduction.

Stock prices are not above the 1936-37 levels, in spite of the fact that in the interim most corporations have added very materially to their assets and to the

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net worth of their stocks. The Council was unanimous in feeling that it would be a very great mistake to establish a 100 per cent margin requirement. That position was taken in the telegram which we sent to the Board and the members of the Council still feel that it would be inadvisable for the Board to take that action.

There has been some discussion in the press--we do not know how well informed it is and would like to be informed--that the Board is considering extending Regulation W to cover improvements on buildings. We think that would be inadvisable in the present situation because we think that credit terms longer than 18 months on improvements are frequently necessary. We would like to know what the present situation is with respect to margin requirements and whether the Board proposes to extend Regulation W in the manner indicated.

We do not believe that a punitive or heavy capital gains tax would be desirable at the present time. We would be opposed to it because we think it would retard the flow of capital into venture enterprises. A good many members of the Council feel that it would be desirable to extend the six-months' period on which capital gains taxes are based, and we all feel that exemption from capital gains taxes now in the present law should be repealed as there have been numerous cases of large amounts of refugee money going into the purchase of buildings and securities which have entirely escaped taxation of any kind.

Mr. McKee inquired whether the Council had considered the advisability of increasing margin requirements to any percentage less than 100 per cent, and Mr. Brown responded that he thought the Council was of the opinion that the present margins were high enough and that an increase would neither deter nor encourage speculation.

In response to an inquiry from Mr. Brown as to whether the Board was still being urged to increase margin requirements to 100 per cent, Chairman Eccles made substantially the following statement:

There are a lot of pressures, not only in the direction of increased margin requirements, but in other directions

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as well. There is a general feeling on the part of those who have responsibility for the stabilization program in Government that the job of holding the line on prices is reaching a point where the pressures can not be withstood much longer. The Office of Price Administration is having an extremely difficult time with black markets expanding and there is an increase in tax evasion. The Department of Agriculture and the heads of all of the farm organizations, as well as the housing authorities, all feel that something has to be done to counteract the inflationary developments that are taking place in the real estate field.

I agree completely with the first part of Mr. Brown's statement and feel that, dealing as we have with the effects rather than the causes of inflation, we have done more than could reasonably be expected for a period of over three years to hold the line as well as we have in the face of a dwindling supply of consumers' goods and a tremendous increase in the purchasing power in the hands of the public. We can not continue to hold the line unless the armed forces are brought to understand the need for real cutbacks and reductions in expenditures and demands on manpower for military purposes. There will also be great pressures on the United States to help relieve the European situation because of the destruction resulting from the war, and we will have to be prepared to send food, raw materials, and machinery over there in order to prevent complete chaos in that area. It seems to me that it would be better to cut back heavily our production for the Japanese war and carry on a war of attrition in that theater in order to meet the pressures at home and afford relief to Europe so that when the war is over we will not be faced with an uncontrollable inflationary situation.

The officials who have responsibility for stabilization in this country are in a difficult position because they have no control over military decisions and, unless public sentiment develops and forces a heavy cutback and a different approach to the war with Japan, we can not avoid a serious situation in this country. The present policy is to conduct an all-out war against Japan so that it can be ended as quickly as possible. That, it is expected, will take 11 million men, huge quantities of

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materials, and heavy casualties among our forces. If the alternative were realized that a war of isolation and attrition would require much less manpower and would permit a more orderly adjustment of the economy in this country so that when the men return from the war they will not be faced with inflation, black markets, and other maladjustments, there would be greater public support for the adoption of that course. Unless something is done in that direction, I do not see how we can prevent the growing inflationary pressures from getting out of hand. That is the situation that the Economic Stabilization Board is facing at the present time.

There is also the pressure right now to do something to meet the situation in the stock market and in the real estate field. There are those who feel that the problem should be dealt with through the credit mechanism, and, inasmuch as an executive order could be issued directing the Board or some other agency to undertake the task, the Board may be faced with the problem of accepting the responsibility or seeing it assigned to some other Federal agency or agencies such as the Securities Exchange Commission, the Farm Credit Administration, or the Federal Housing Administration. There are objections to granting to these agencies the powers to regulate credit and if the responsibility is to be undertaken it probably should be placed in the Board. As you know, I feel that regulation of the use of credit is not the way to get at inflation and that an effective capital gains tax would be a much more effective instrument. There is a feeling that it would be impossible to get an adequate capital gains tax, but that authority to regulate credit in the real estate field could be obtained. For that reason, the pressure is in the direction of credit regulation as something that is readily available. I think we are likely to get one or the other.

If the Council has any suggestions as to how substantial cutbacks in military expenditures and demands for manpower for the services could be brought about the Board would be pleased to receive them.

Mr. Brown inquired whether the Board had stated its position that there should be substantial cutbacks in military expenditures,

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and Mr. Eccles responded that it had not.

Mr. McKee suggested that, in view of the substantial agreement between the Council and the Board on the necessity for such cutbacks, the Council might consider adopting a resolution with respect to it.

Mr. Brown inquired whether, if that were done, the Board would concur in it, and several members of the Board indicated a feeling that it would of course depend on how far the statement went, but that a resolution could be drafted that could be agreed upon. Mr. Brown stated that everything possible should be done to present the picture to Congress, as only Congress or the President could make the necessary decisions.

Mr. Ransom suggested the advisability of asking Secretary Stimson and General Marshall to meet with the Board and the Council to explain the views of the Armed Services as to the present strategy in the war with Japan. After hearing these gentlemen the Council and the Board could explain their reasons for thinking that cutbacks in military expenditures might be desirable if the general strategy permitted, in order to minimize inflationary possibilities.

Mr. Brown stated that he would like some assurance that if the Council adopted a resolution the Board would take a similar position.

Chairman Eccles stated that the Board was in a somewhat different

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position from the Council which represented a private point of view, whereas the Board was a part of the Government and under the present arrangement would not be at liberty to make a public statement on a matter of this kind without clearing it with the Office of War Information.

Mr. Ransom suggested that if a resolution were prepared the Board could ascertain whether it was acceptable and, if not, why not.

Chairman Eccles referred to informal discussions which he had participated in recently in high official circles, in which he took the position that there should be substantial cutbacks in military expenditures, and stated that up to the present time he had not been able to get effective acceptance of his position.

Mr. Brown called on the members of the Council for their views with regard to the suggested resolution by the Council.

Mr. Kurtz doubted whether much attention would be paid to such a statement. However, he did think it was highly important that something be done to meet the problem, that if all the facts were known there would be wide public acceptance of a program of cutbacks as an insurance against the servicemen returning home to find their country in the throes of inflation and black markets.

Mr. Gifford did not know what good a statement by the Council would do, but if it would do any good he would not object.

Mr. Berry asked what the effect would be if the Board submitted

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its opinion on the matter to the proper authorities. He thought that that might enable these authorities to try to deal in fundamentals rather than to approach the matter through credit control or some other method that did not solve the problem, and that such a procedure might have more effect than a statement from the Council.

Mr. Winton expressed the opinion that the Council should give the Board the support that it needs in this matter. He said that with the exception of the capital gains tax he agreed fully with the position stated by Chairman Eccles and that if the Council should elect to make a statement he would favor the suggestion made by Mr. Ransom of inviting representatives of the armed forces to discuss the matter and to state their reasons why a program of substantial cutbacks should not be adopted. If, he said, adequate reasons were given for the present program which requires an armed force of 11 million men and an expenditure of \$70 billion a year, the Board and the Council would want to concur but in the absence of such reasons the Council's statement could be adopted to support the Board in its position as to the steps that should be taken.

The suggestion of a conference with representatives of the armed forces was discussed and it was agreed that it should not be undertaken at this time.

Mr. Baird stated that he would be willing to issue a statement if it would do any good but he was not sure that it would



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accomplish anything and might be misinterpreted as an effort to "let the boys down in the field." He was satisfied that if the public understood what the alternatives were it would not favor the present policy of all-out-war, that there should be some way of marshaling that sentiment and that if the members of the Council talked to the members of Congress from their respective States, it might be that they could do some good.

Chairman Eccles agreed that it might be very helpful if the members of the Council would discuss the matter with the Senators from their respective States, pointing out the possible alternatives and the fact that, because of the inflationary dangers involved in the present policies, this country might win the war on the battle front but lose it on the home front. He also read a portion of the current Whaley-Eaton letter as indicating some feeling on the part of the public that there is another way to fight the war than on an all-out basis, and that, if the public and Congress realized that, the armed services would change their position.

Mr. Kurtz made the additional suggestion that, if two or three of the leading newspapers would comment editorially on a statement from the Council, the statement would then be very much worth while.

Mr. Wallace raised the question as to how the problem under discussion might be presented effectively to the President and suggested that that would be the best way to start. He doubted the

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wisdom of the Council issuing a statement on the matter and inquired why, if the Board did not think credit regulation was an effective way to meet the problem, it would be willing to undertake such regulation.

Chairman Eccles said that it was a question of alternatives and that his personal opinion was that the best way to meet the existing pressures was through the medium of taxation.

Mr. Wallace felt that to increase margin requirements to 100% would have a bad effect, as it would result in liquidation of Government securities to enable the holders to purchase stocks for cash.

Chairman Eccles commented that there was a difference of opinion on that point, since there was only a relatively small amount of credit being used in the stock market. He also said that the reason why the Board was being put under pressure to increase margin requirements was that the position had been taken that Congress should not be asked for additional authority when existing authority had not been used and that it did not help the situation merely to assert that the exercise of the existing authority would not accomplish anything material.

Mr. Traphagen said he would be very sorry to see the Board exhaust its authority to increase margin requirements, because he thought such action would have just the opposite effect from that intended. He thought the known fact that the Board could increase margin requirements at any time was, in itself, quite a deterrent. Furthermore, he did not think the market was getting out of hand, as prices were

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still 15 per cent under their 1936-1937 highs, notwithstanding the fact that the market was reflecting the stronger financial position of the issuing companies and the low level of money rates. On the question of a statement by the Council, he was opposed to such a statement at this time. He could not help but feel that the armed services want to show that this country is wholeheartedly back of the war and would bring all of its strength to bear against the Japanese, with the result that the Japanese Government might surrender. It was his feeling that a statement on the part of the Council would not be understood and would not accomplish the desired result.

Mr. Szymczak inquired whether the statement might not be used by the Chairman in his meetings with Messrs. Vinson and Davis who might be in a position to carry it further.

Mr. McKee stated that the Council would not meet again until September and that the Council might consider adopting a statement at this time with the understanding that it might be used as Mr. Szymczak indicated or released at a later time if that should be thought to be desirable.

Mr. Winton said that was exactly what he had in mind.

Mr. Traphagen thought that much more could be done if members of the Council would talk to individuals in influential places.

In the discussion which ensued as to the publication of a statement by the Council, the opinion was generally concurred in that

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if adopted the statement should not be released to the press at this time.

Mr. Bradshaw said that he agreed with the position which had been taken by Mr. Traphagen.

Mr. McCoy thought that the Council should adopt a statement, not for release to the press but to be given to the Board for use where it could be used to advantage. He thought that the members of the Council should support the Board in this matter in every way they could including discussing the matter with members of the Senate.

Mr. Bradshaw thought that the talks with members of the Senate was the better approach.

Mr. Eccles suggested that the Council might give the Board a statement so that it might be available for discussions which he might have with Messrs. Davis and Vinson, General Somervell, and other authorities who have responsibility for the adoption of policy. He thought that such a statement would be entirely appropriate in view of the Council's responsibility as advisers to the Board. He added that he would like to see the Council also suggest that there be a substantial extension of the period during which capital assets are held subject to the capital gains tax.

Mr. Winton agreed with all that Chairman Eccles had said except that he would not include in the Council statement any reference to a capital gains tax. He thought that it would be bad

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psychology to bring up the question of an extension of the holding time as it would open the whole question of capital gains tax, and the other objectives sought to be accomplished by the Council's statement, which were much more important, might not be achieved.

Chairman Eccles stated that substantial cutbacks in military expenditures would be effective in meeting the situation in connection with consumer goods but would not stop inflationary pressures in the stock market and in real estate, and that, therefore, something in addition to cutbacks in military expenditures was necessary.

Following a discussion of conditions now existing in the stock market and of possible effects of action by the Board to increase margin requirements, Mr. Beal said he could not agree that the market had gone up because of any cause other than supply and demand. He also said that, in the investment of trust funds, banks and trust companies had been forced out of the purchase of corporate bonds and the only way left of investing funds at a reasonable rate was to invest part in Government bonds and part in stocks. He felt that the rise in the stock market was due to that situation rather than to speculation. With respect to the proposed statement by the Council, Mr. Beal thought there should be some way to make known the inflationary dangers of the present program for the Japanese war and that the Board and the Council would be in a weak position if they did nothing.

Mr. Rieman did not think the public would be in favor of an all-out war against Japan if they realized that it would mean greater

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restrictions when the war was over. He was of the opinion that it would be proper for the Council to adopt a resolution which would lay down certain sound principles and that because of the importance of the matter it would be bad for the Council to remain silent. He felt it would be a mistake to raise margin requirements, because the unused power of the Board was a continuing threat of action and if all of the authority were used now the Board would have nothing left to meet further developments. He did not think there was anything to worry about in the stock market at the present time.

Mr. Brown stated that there were other matters to be discussed with the Board, and that the Council would meet after lunch for the purpose of considering the adoption of a statement along the lines suggested.

He then referred to the bank holding company bill recently introduced in Congress and stated that, while the Council as such had taken no position on the question whether a bank holding company bill should be introduced at this time and if it were introduced whether it should undertake to freeze the existing situation as the bill now before Congress would do or whether it should contain a death sentence, a majority of the Council felt that a bill which would freeze the existing situation would be preferable. There were two points with respect to the existing bill, he said, on which members of the Council felt very strongly. The first of these was the definition of a bank holding company to include "any group of persons that, after notice

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and opportunity for hearing, the Board has determined exercises such a controlling influence over the management or policies of two or more banks by means of joint or concerted action or pursuant to a mutual understanding or arrangement as, in the public interest, to require such person or group of persons to be subject to the obligations, duties, and liabilities imposed upon bank holding companies."

Mr. Brown said that, while the Council realized the difficulty of definition, it was opposed to giving the Board or any other administrative body such a "dragnet" authority in the absence of more adequate provision for review of the Board's findings. He went on to say that the definition would cover a large number of institutions not now regarded as holding companies; that the present definition was very different from the definitions contained in earlier drafts of the bill, and that the Council felt that, if some other method of definition could be found which would afford a much more specific legal test, it would be desirable.

The other objection of the Council to the present bill, Mr. Brown said, was that it would operate to prevent industrial concerns from lending financial assistance to banks in times of emergency and that it was believed that this would be a most undesirable situation. He added that some of the existing bank holding companies felt that there were certain other minor technical details in the bill that should be changed and that the Council would like to know what the

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present plans were for hearings on the bill and to what extent it had the support of other agencies of Government.

Chairman Eccles stated that, so far as he knew, no program for hearings had been agreed upon; that there were a number of other very important bills before the Senate and House Banking and Currency Committees, and that he did not know when the bank holding company bill would be taken up if it were taken up at all. He then outlined briefly the extent to which the bill had been cleared with other agencies of Government stating that so far as he knew the Treasury still favored the death sentence and had reserved the right to propose amendments to the present bill when it came up for hearings. It was his opinion that the death sentence would not meet the problem for the reason that it would not affect in any way groups which were operating banks as individuals. He also said that failure to get legislation at this session of Congress would serve to put a stamp of approval on what was being done by bank holding companies; that the present favorable investment position of bank stocks was an invitation to increase the number of bank holding companies, and that the Board was without adequate authority to do anything about it in the absence of the enactment of additional legislation. He made the further comment that if Congress did not see fit to grant the Board additional authority there was nothing the Board could do but to let the matter take its own course, and that he was not inclined to undertake a fight for the legislation.



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Mr. McKee stated that the definition contained in the bill had been worked out carefully in the light of the Board's experience with the existing bank holding company legislation with full knowledge of the matters which the members of the Council had in mind. He also said that the definition was necessary to prevent practices which had been resorted to in the past which were not only harmful to bank holding companies but to independent banks as well. It was Mr. McKee's opinion that if the bill proposed by the Board was not enacted a bill containing a death sentence would be passed, that the Board had done all it could to meet the situation, and that if the proposed legislation were not enacted the responsibility would rest elsewhere than on the Board.

In response to a comment by Mr. McKee that he could not visualize a situation in which the holding company bill would be administered in such a way as to prevent financial assistance being rendered to banks by large industrial concerns in the event of an emergency, Mr. Brown stated that as long as the proposed bill was on the statute books industrial concerns would not invest in bank stocks at the expense of becoming subject to the limitations imposed by the bill on bank holding companies.

Mr. Eccles outlined the reasons why, in his opinion, it was undesirable for business concerns to invest in bank stocks and why emergency capital requirements of banks should be met in some other manner.

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Mr. Brown expressed the wish that the Board would be willing to afford an opportunity to discuss the definitions of a bank holding company which were in earlier drafts of the bill.

Chairman Eccles commented that the earlier drafts were inadequate and that the present definition was the result of further consideration.

Mr. Brown said that it seemed to him that a revision of the definition was desirable and Chairman Eccles suggested that the Council submit a draft of definition which would be acceptable to it, and stated that the Council would have full opportunity to express its views when hearings were held on the bill.

After some further discussion Mr. Brown stated that the Board had asked for the views of the Council with respect to the practice followed by certain large depositors of asking the depository banks for more detailed information regarding the condition of the banks than is shown in their regularly published reports of condition. He said that the Council did not think that the practice was a very serious one, that eight members of the Council were opposed to the imposition of any prohibition by law or regulation upon banks giving any information that they wanted to give to their depositors, that two members were in favor of such a prohibition, and that Messrs. Beal and Rieman, who were not regular members of the Council, did not vote.

Mr. McKee read the statement appearing on the cover of each

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report of examination made by examiners for the Federal Reserve System which contains the statement that under no circumstances shall the bank or any of its directors, officers, or employees, disclose or make public in any manner the report of examination or any portion thereof.

He said that similar statements were contained on the covers of reports of examination made by the office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation, that in the future State member banks would be asked to acknowledge receipt of the report of examination as being subject to the understanding set forth in the statement, and that this was a protection to the bank against having to give special information in response to requests from their depositors.

Mr. Gifford stated that none of the questionnaires he had seen asked for information contained in reports of examination, whereupon Mr. McKee read from a questionnaire form received by one bank which, among other things, called for the classification of assets according to the last examination.

Mr. Traphagen said that he had never seen a request of that kind and expressed the opinion that one depositor should not be given more information than was given another.

Mr. Winton stated that his bank had received a questionnaire of the kind referred to by Mr. McKee and had declined to give the information.

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Mr. Brown stated that the Board had also asked the Council for its opinion as to the progress being made by "credit pools" organized by banks in various sections of the country upon recommendation of the American Bankers Association, and that the Council felt that the establishment of the pools had been a good thing but that as yet they had not done much business.

Thereupon the meeting adjourned.

Chester Morris  
Secretary.

Approved:

W. S. ...  
Chairman.