

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, November 19, 1945, at 10:30 a.m.

PRESENT: Mr. Eccles, Chairman
Mr. McKee
Mr. Draper
Mr. Evans

Mr. Carpenter, Secretary
Mr. Hammond, Assistant Secretary
Mr. Connell, General Assistant,
Office of the Secretary
Mr. Thurston, Assistant to the Chairman
Mr. Morrill, Special Adviser
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. Bethea, Director of the Division
of Administrative Services
Mr. Brown, Assistant Director of the
Division of Security Loans

Messrs. Spencer, Kurtz, McCoy, Fleming,
Berry, Brown, Gifford, Baird, Bradshaw,
Winton, and Wallace, Members of the Fed-
eral Advisory Council from the First,
Third, Fourth, Fifth, Sixth, Seventh,
Eighth, Ninth, Tenth, Eleventh, and
Twelfth Federal Reserve Districts, respec-
tively

Mr. S. Sloan Colt, alternate for Mr. John C.
Traphagen representing the Second Federal
Reserve District

Mr. Prochnow, Acting Secretary of the Federal
Advisory Council

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Mr. Brown expressed appreciation of the assistance given by the Board and its staff in presenting to the Treasury the recommendation adopted by the Federal Advisory Council that the present procedure for the licensing of national banks and State member banks pursuant to Presidential Proclamations of March 6 and March 9, 1933, and Executive Order of March 10, 1933, be terminated. He said that Mr. Fleming, who had handled the matter for the Council, had reported that Secretary of the Treasury Vinson apparently was agreeable to the proposal and that it appeared that it would be approved.

In response to Mr. Brown's inquiry as to whether the Board knew of any developments in connection with the recommendation, Chairman Eccles said that Comptroller of the Currency Delano had stated that Secretary Vinson had talked to him about the matter, that there appeared to be no objection to the recommendation, and that he thought it would be adopted.

Mr. Fleming stated that he did not see how the Board could have endorsed the recommendation in any stronger terms. He also said that it was his understanding that the matter had been placed in the hands of Messrs. Delano and Under Secretary Bell to handle.

Mr. Brown inquired whether the Board had any information as to the status of the Reorganization Bill now before Congress which would authorize the President to reorganize certain of the executive departments and agencies of the Federal Government. Chairman Eccles

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stated that the Board had no information beyond that available in the press, that the bill had not yet passed the Senate, and that any action taken in connection with it would be for the Administration to determine.

The comment was made by Mr. Brown that the Council understood that the Bank Holding Company bill which had been submitted to Congress by the Board in March of this year had been withdrawn.

Chairman Eccles replied that the bill had not been withdrawn by the Board. He also said that Congressman Spence, Chairman of the House Banking and Currency Committee, had been urged by representatives of the independent bankers group to hold hearings on the bill, that he had suggested to Chairman Spence that he defer hearings for the time being, and that he (Chairman Eccles) would like to undertake the preparation of a draft of bill which would have some chance of approval. He added that he was convinced personally that the present bill could not be defended, that he had discussed the draft with representatives of the Treasury and was advised that the Treasury would oppose it, and that it was apparent that it had no possible chance of approval. He went on to say that there had been some discussion of the matter with representatives of the Treasury, and the Attorney General who was interested in the monopoly aspects, that it was expected that it would be known shortly whether it would be possible to propose a bill which the Treasury and the Department of Justice would support, and that if so, he, Secretary Vinson, and Attorney General Clark, would join in

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getting Administration support of the measure. It was Chairman Eccles' opinion that it was a waste of time to urge the passage of bank holding company legislation in any form which did not have such support and that it would be impossible to get that support for the present bill. He said that he had submitted a draft of a substitute bill to the Board and at the same time had sent copies to the Treasury and Justice Departments for study while it was being considered by the Board and that it was being studied by members of the staff of the two departments. He did not know what the outcome of the matter would be. He made it clear that the Board had taken no action on the revised bill, as such, but that it had approved the submission of the revision to the Treasury and Justice Departments.

Mr. Brown asked if it would be possible for the members of the Council to see a copy of the bill or whether the Board would be willing to tell the Council the general theory on which the bill was based.

Chairman Eccles responded that he thought it would be inadvisable for the Board to submit the draft to outside parties before it was sent to Congress.

Mr. McKee made the statement that the bill now before Congress had been prepared on the basis of the Board's experience under its existing supervisory authority over bank holding companies and he did not think it would be difficult for the Board to testify on the bill because it had had experience with each of the conditions that would

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be imposed by the measure. He referred to the bank holding company bills which had been before Congress in recent years and the consideration that had been given to them, pointing out that the Board had not favored a bill containing a "death sentence". He expressed the opinion that the application of a death sentence would have serious results in certain sections of the country. Following the introduction of the bill proposed by the Board, Mr. McKee added, the independent bankers had accepted the idea of freezing the existing situation and were prepared to support that position. He went on to say that there had been considerable pressure for hearings on the Board's bill, that such hearings had not been held, but that the bill had not been withdrawn by the Board and he had not changed his mind as to the approach that should be made to the problem of bank holding company legislation and felt that it would be well to have hearings. He also felt that if the present bill were withdrawn, "death sentence" legislation would result because the independent bankers would not be willing to support a bill along the lines being suggested by Chairman Eccles.

There was a brief discussion of the two points of view expressed by Messrs. Eccles and McKee.

Mr. Brown then referred to the question presented by the Board as to the best way to meet the issues which might be raised in connection with the cost of the Government debt with particular

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reference to that part of the debt held by banks, and stated that the Council understood that Congressman Patman had a bill with respect to bank earnings ready for discussion as soon as the Victory Loan drive was out of the way. He said that none of the members of the Council had seen the bill or knew what it or other bills along the same lines might propose and that, therefore, it was difficult to say what the opinion of the Council was as to the measures that should be taken to meet the issues that might be raised. He added that Council would strongly urge that the Board of Governors make a study of bank earnings, including a forecast of what such earnings might be during the next five years. In this connection, he said that the members of the Council were unanimous in their feeling that salaries and other operating costs of banks were increasing at the present time and would continue to increase for several years, that many of the Government securities now in the banks' portfolios would be refunded at much lower rates, and that they foresaw a steady decline in the rate of income from Government security holdings. He made the further comment that when the issues which were not now eligible for bank investment become eligible the demand for such issues would result in such a low yield that they would not help the earning picture materially. Furthermore, the Council could see little likelihood of any substantial increase in demand for credit from private sources which would raise the level of bank earnings.

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With respect to the study referred to by Mr. Brown, he said that the Council felt that if such a study were made by the American Bankers Association it would not be accepted, that if it were made by an organization such as the Brookings Institution there would be less chance of its being accepted than if it were made by an agency such as the Board of Governors, and that inasmuch as the Board had all of the basic information it should undertake such a study.

In response to Mr. Brown's inquiry, Mr. Thomas stated that the Board's staff was working on the problem.

There was a discussion of the points that should be taken into consideration in making the forecast proposed by the Council and Mr. Brown inquired whether the Board had received any indication of the form of the legislation that might be introduced by Congressman Patman or others on this subject. Chairman Eccles replied in the negative, and stated that instead of introducing legislation the Congressman might ask for a resolution authorizing an investigation to develop the facts with respect to the ownership of the public debt, how the banks create funds with which to purchase Government securities, and the effect of their Government security holdings on bank earnings.

Chairman Eccles then discussed the problems associated with the large Government debt as he saw them and why the management of the large outstanding debt, rather than the demand for private credit,

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would be the controlling element in the determination of interest rates for many years to come. In this connection, he pointed out that the banks by purchasing long-term governments were forcing the rates down and that the level of yields on Government securities were affecting the yields on private issues as well. This grew out of the fact, he said, that the banks were buying governments which were eligible for bank purchase away from insurance companies and other institutional investors and these institutions were forced to purchase non-eligible issues which, when they became eligible for bank purchase, would be in such demand that they also would be sold at a premium and at reduced yields. He thought that it was unfortunate that the long terms were ever made eligible for bank purchase, that failure to make them ineligible would continue to force yields down, and that there was nothing that could be done to stop that trend. He stated that the reduction of taxes and the continuation of Treasury deficits would only tend to aggravate the problem.

In response to inquiry by Mr. McKee, there was a discussion of what might happen to short-term Government securities now held by corporations and it appeared to be the consensus of the members of the Council that the tendency would be for them to find their way into the banks.

With further reference to the suggestion that the Board make a study of bank earnings, Mr. Brown said that a Congressional

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investigation of the whole situation, based on the true facts that such a study would make available, might be a desirable thing.

Mr. McKee said that it would take time to make a complete study and that it might not be available by the time Congressional hearings were held. Mr. Brown inquired how long the study would take and Mr. Thomas said that something could be ready by January but that it might not be complete and comprehensive.

Mr. Brown then stated that the members of the Council, with one exception, felt that, in the face of the very acute housing shortage, it was absolutely necessary to keep rent controls in effect for sometime to come but that they were opposed to the suggestion of the Office of Price Administration that ceiling prices be established on either existing or new construction. In response to his inquiry whether the Board had thought of any program which would deal with this very serious problem, Chairman Eccles said that the matter had been discussed at meetings of the Economic Stabilization Board, that in his opinion it had been a mistake to remove the controls on building materials and to discontinue the issuance of permits for new construction, that there was nothing that could be done now, and that in his opinion there would be an uncontrolled black market in such materials. He felt that there was no purpose in trying to control the prices of materials if there were no control of the prices at which the finished building could be sold.

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Mr. McKee asked if the members of the Council had any suggestions as to a way by which permits for new construction could again be required but the members of the Council had no comment.

Chairman Eccles said there was also the question whether returning servicemen should incur mortgage debt on houses purchased at the present high prices, that while the veteran organizations were pressing for action to meet the situation there did not appear to be anything that could be done, and that even if there were an executive order or legislation requiring large down-payments, that would not help those in need of housing who do not have the down-payment. While he thought the problem might be helped by requiring an official appraisal and a down-payment on the basis of that appraisal, such a requirement would be very difficult to administer.

Mr. Brown then asked if there were any way, through the use of financial controls, by which the present rapid inflationary trend resulting from demands for increased wages could be held in check, and stated that the members of the Council did not see that anything could be done by that means.

Chairman Eccles expressed the opinion that the opportunity to do anything in that field was lost when the excess profits tax was repealed and the War Labor Board was discontinued and that the capital gains tax which he had proposed would have been effective in reducing the speculative pressure on prices. He pointed out that conditions

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were not any different from the standpoint of inflationary pressures after the war than before its termination, and that controls were discontinued at a time when they were more necessary than ever before, with the result that after effectively controlling prices during the war a serious inflationary situation was being allowed to develop in the reconversion period.

In the discussion of this matter there was agreement that the situation called for action by Congress and that the question whether legislation would be passed would depend on whether public sentiment would demand such action.

Mr. Berry expressed the view that the Government attitude on wages and the fiscal policy of the Treasury was providing impetus to the inflationary trend, that the problem should not be approached from the standpoint of interest cost alone as there were other elements of cost, and that it seemed to him that there should be some effort to place a larger portion of the Government debt in private hands even at a higher interest rate.

Following a comment by Mr. Colt that when the present large productive capacity of the United States went into operation he would not be much concerned about inflation, Chairman Eccles commented that it was a question of timing, and that if the line had been held until reconversion had been accomplished controls could have been released and the supply of goods would have taken care of the situation. He

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also said that how long it would take for the supply of goods to catch up with the demand was an important question, that there would be shortages of certain things such as housing, and that the time it would take to meet the backlog of demand would depend on a solution of the labor problem and what the policy was to be with respect to exports.

Mr. Berry said that on the assumption that prices would be maintained and production increased to meet the demand, the increased production would provide additional purchasing power and, therefore, would not reduce inflationary pressures.

Chairman Eccles responded that adequate production would take the pressure off prices and that past experience, particularly during the depression, had demonstrated that purchasing power created by production would not result in pressure for higher prices.

Mr. Brown asked how strict the existing controls were on export licenses and Chairman Eccles replied that the policy was a strict one with licenses being granted only when the exporter could show (1) that he had the goods and would not have to go into the market and bid for them, (2) that the goods could be spared, and (3) that they were needed abroad.

Mr. McKee stated that Mr. Kurtz had raised the question as to the application of the limitation established by the Treasury during the Victory Loan drive on war loan deposit accounts under which such

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accounts could not exceed 30 percent of the total deposits of the bank exclusive of war loan deposits and whether the limitation would result in any change in the basis upon which war loan deposits would be withdrawn by the Treasury. With respect to the latter point, Mr. McKee said he had discussed the matter with Mr. Bell, who said that withdrawals would continue to be made on the same basis as in the past. He also said that there was a question whether the payments for securities made by the banks when their war loan accounts had reached the limit would create a money market situation which might cause difficulty.

Mr. Brown thought that there was no possibility of a situation of that kind arising and that the limitation was a good way to prevent the abuses that had occurred in the past. Other members of the Council concurred in Mr. Brown's opinion and Chairman Eccles suggested that the Council adopt a resolution to that effect and stated that, if the other members of the Board agreed, he would be willing to transmit such a resolution to the Treasury.

In connection with a reference to the authority of the Federal Reserve Banks to purchase Government securities directly from the Treasury under the provisions of Section 14(b) of the Federal Reserve Act as amended by Title IV of the Second War Powers Act, Chairman Eccles said that the Board had not undertaken to get a separate bill for renewal of the authority as it was felt that there was a greater

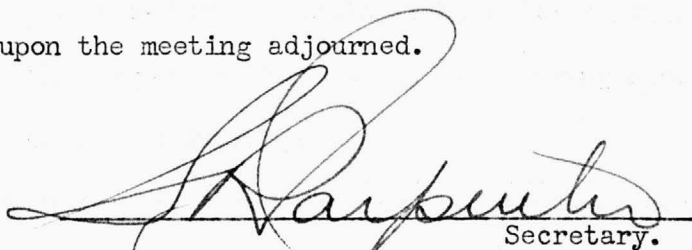
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likelihood of a renewal as a part of the bill extending certain of the provisions of the Second War Powers Act which was being handled by the Office of War Mobilization and Reconversion. He also said that the Board and the Treasury felt, for reasons which he outlined, that the law should be amended to restore the authority of the Federal Reserve Banks to purchase securities directly from the Treasury in the form in which it existed prior to 1935. He pointed out that the continuation of the authority would not affect the amount of securities held by the Federal Reserve Banks and that the only question involved was whether the securities could be purchased direct or whether they would have to be acquired in the market, in which event the Federal Reserve Banks would have to pay the usual commissions.

Mr. Fleming inquired whether there was any thought of abandoning the 3/8 percent option rate on Treasury bills, to which the Chairman responded that as soon as the Victory Loan drive was over the whole question of open market policy would have to be reviewed.

Thereupon the meeting adjourned.


Secretary.

Approved: 
Chairman.