MINUTES OF MEETING

of the

FEDERAL ADVISORY COUNCIL

November 17-19, 1940

MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

November 17, 1940

The fourth statutory meeting of the Federal Advisory Council for 1940 was convened in Room 936 of the Mayflower Hotel, Washington, D. C., on Sunday, November 17, 1940, at 2:00 P. M., the President, Mr. Brown, in the Chair.

Present:

Mr. Thomas M. Steele	District No. 1
Mr. Leon Fraser	District No. 2
Mr. Howard A. Loeb	District No. 3
Mr. B. G. Huntington	District No. 4
Mr. Ryburn G. Clay	District No. 6
Mr. Edward E. Brown	District No. 7
Mr. S. E. Ragland	District No. 8
Mr. John Crosby	District No. 9
Mr. John Evans	District No. 10
Mr. Paul S. Dick	District No. 12
Mr. Walter Lichtenstein	Secretary

Absent:

Mr. Robert M. Hanes	District No. 5
Mr. R. Ellison Harding	District No. 11

On motion, duly made and seconded, the minutes of the Council meeting of October 6-8, 1940, copies of which had been previously sent to the members, were approved.

The Secretary stated that Mr. Harding expected to arrive later in the afternoon and that Mr. Hanes planned to arrive tomorrow.

Mr. Fraser reported for the Special Committee on "Easy Money" Policy. He explained that it had been found necessary to postpone the meeting with a committee of the Board of Governors which had been originally set for Friday, November 15, 1940. It was now planned to have the meeting of the two committees take place in the afternoon of Monday, November 18.

Mr. Fraser reported at length regarding a conversation he had had in New York last week with Chairman Eccles, in which the latter had outlined a proposal for a comprehensive statement dealing with financial and fiscal policies to be prepared under the direction of the Board of Governors, and which conceivably might be submitted to Congress and concurred in by the Federal Advisory Council and the Conference of the Presidents of the twelve Federal Reserve Banks.

Mr. Steele read a memorandum in which he argued that the statement of the Board might be more effective if it were presented independently and without any cooperation on the part of the Federal Advisory Council.

Mr. Brown summed up the discussion as follows:

(a) Can the Council agree with the Board of Governors and the Federal Reserve Banks on a general statement which obviously would have to consist of generalizations, such as that it is desirable to have United States bonds bought by private investors, that it is necessary to balance the budget, etc., without becoming more specific?

(b) Assuming there was an agreement on a very general statement, would it have any effect on public opinion and on Congress?

(c) It is necessary to answer questions (a) and (b) before the Council can decide whether or not it would be best to suppress its statement on "easy money" and become a party to a general statement such as has been outlined.

At 2:45 P. M. Mr. Harding joined the meeting.

At 3:00 P. M. Mr. J. O. Brott, Assistant General Counsel of the American Bankers Association, joined the meeting in order to discuss the topic placed on the agenda by Mr. Huntington, dealing with the tax treatment of charged-off assets and recoveries of banks and the tax treatment of gains and losses resulting from the sale of capital assets by banks. Mr. Brott stated that a committee of the American Bankers Association was discussing these problems with the proper officials of the Internal Revenue Bureau and it was hoped to obtain a ruling on these problems in the near future. Mr. Brott left the meeting at 3:30 P. M.

After some discussion it was decided that it would be inadvisable for the Federal Advisory Council to approach the Board of Governors on a matter which dealt with administrative details of another Department of the Government and that it would be better to let the American Bankers Association, the Comptroller's office, and the Federal Deposit Insurance Corporation handle these matters.

On motion made by Mr. Steele, and seconded by Mr. Loeb, the following resolution was adopted:

"It was voted unanimously that the Federal Advisory Council adopt the general practice of giving to the press, after each meeting, a statement by its President. It is intended that this statement be general in its terms, unless for some special reason it should be thought best to go into details. It is expected that ordinarily, before issuing a statement, the President of the Council will consult with the Chairman of the Board of Governors or such representative of the Board as the Chairman may designate. It is not intended to change hereby the procedure governing the publication of the Council's resolutions or recommendations as fixed by a resolution adopted on November 20, 1934, by the Federal Advisory Council in agreement with the then existing Federal Reserve Board.

"The resolution of November 20, 1934, read as follows:

'It is the opinion of the Federal Advisory Council as at present constituted that when the Council desires to give publicity to its proceedings it should, by itself or through its representatives, discuss such resolutions or recommendations with the Federal Reserve Board and request that these be given publicity. A reasonable opportunity should be given to the Federal Reserve Board to consider and comply with the request of the Council, and the Council itself should not give publicity to its resolutions or recommendations unless the Board, after due consideration, should be unwilling to comply with the request of the Federal Advisory Council to give the desired publicity.' "

The meeting adjourned at 5:45 P. M.

WALTER LICHTENSTEIN,
Secretary

MINUTES OF JOINT CONFERENCE OF THE FEDERAL ADVISORY COUNCIL AND THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

November 18, 1940

At 10:30 A. M. a preliminary joint conference of the Federal Advisory Council and the Board of Governors of the Federal Reserve System was held in the Board Room of the Federal Reserve Building, Washington, D. C.

Present: Members of the Board of Governors of the Federal Reserve System:

Chairman Marriner S. Eccles; Vice Chairman Ronald Ransom; Governors M. S. Szymczak, John K. McKee, Chester C. Davis, and Ernest G. Draper; also Messrs. Lawrence Clayton, Assistant to the Chairman of the Board of Governors; Elliott Thurston, Special Assistant to the Chairman of the Board of Governors; Chester Morrill, Secretary of the Board of Governors; S. R. Carpenter, Assistant Secretary of the Board of Governors; and E. L. Smead, Chief of the Division of Bank Operations.

Present: Members of the Federal Advisory Council:

Mr. Edward E. Brown, President; Mr. Howard A. Loeb, Vice President; Messrs. Thomas M. Steele, Leon Fraser, Robert M. Hanes, Ryburn G. Clay, S. E. Ragland, John Crosby, John Evans, R. Ellison Harding, Paul S. Dick, and Walter Lichtenstein, Secretary.

The President of the Council stated that the Council would be glad to hear anything the Board wished to say concerning problems of financing the defense program, since it was indicated in a letter from the Secretary of the Board of Governors, dated November 1, 1940, and addressed to the Secretary of the Council, that the Board wished to discuss this with the Council and special mention was made of "a plan designed to increase the participation of small business enterprises in the program." Vice Chairman Ransom suggested that Governor Draper bring the members of the Council up to date.

Governor Draper thereupon presented the plan under which the Federal Reserve banks and branches would act as centers of information in respect to Government contracts in order that the small business men might be able to obtain proper legal and other assistance and not be compelled to travel constantly to Washington. It was not intended in this way to bring added business to the Government agencies, but rather to assist small business men to obtain financial assistance from the commercial banks.

Governor Davis pointed out that it was desired to use the productive capacity of every part of the country and to decentralize, as far as possible, the handling of armament contracts. The Federal Reserve System had about 36 offices spread throughout the country and specially designated men in each such office would be asked to familiarize themselves with the various details of the defense problems. In further discussion, it was pointed out by various members of the Board that by this plan it was hoped to utilize resources scattered over the country and thus prevent bottlenecks in production. It was not intended in any way by this program to increase loans made under Section 13b of the Federal Reserve Act. The initiative for this plan came from the Advisory Commission to the Council of National Defense, and not from the Federal Reserve System.

The President of the Council stated that the banks were desirous of assisting in every way possible.

Chairman Eccles then presented his plan for having a statement prepared in which the Federal Advisory Council and the Federal Reserve Banks might concur, this statement to be presented to Congress.

The President of the Council stated that it might be difficult to obtain an agreement if the statement went into detail but it might be possible to obtain a useful statement, general in its terms, in which the various constituent parts of the Federal Reserve System might concur. It was also conceivable that the statement might consist of two separate parts, one of which would be agreed to by the Council and the Federal Reserve banks, while the other part would be a statement supported only by the Board of Governors and not concurred in by the Council and the Federal Reserve banks.

The members of the Council agreed that it would be desirable to have the committee of the Council appointed for this purpose meet with a committee of the Board of Governors to consider the possibility of an agreement and the procedure to be followed.

The meeting adjourned at 1:00 P. M. and the Council had lunch with the Chairman of the Board of Governors.

WALTER LICHTENSTEIN,
Secretary

MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

November 18, 1940

At 2:15 P. M. the Federal Advisory Council reconvened in the Board Room of the Federal Reserve Building, Washington, D. C., the President, Mr. Brown, in the Chair.

Present: Mr. Edward E. Brown, President; Mr. Howard A. Loeb, Vice President; Messrs. Thomas M. Steele, Leon Fraser, Robert M. Hanes, Ryburn G. Clay, S. E. Ragland, John Crosby, John Evans, R. Ellison Harding, Paul S. Dick, and Walter Lichtenstein, Secretary.

The Council listened to a discussion of business conditions presented by Dr. E. A. Goldenweiser, Director of the Division of Research and Statistics of the Board of Governors, in which it was pointed out that there had been a very large increase in production and that there were no evidences that there is likely to be a drop in the near future.

Dr. Goldenweiser left the meeting at 3:00 P. M., after which the Council adjourned.

WALTER LICHTENSTEIN,
Secretary.

MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

November 18, 1940

At 6:00 P. M. the Federal Advisory Council reconvened in Room 936 of the Mayflower Hotel, Washington, D. C., the President, Mr. Brown, in the Chair.

Present: Mr. Edward E. Brown, President; Mr. Howard A. Loeb, Vice President; Messrs. Thomas M. Steele, Leon Fraser, B. G. Huntington, Robert M. Hanes, Ryburn G. Clay, S. E. Ragland, John Crosby, John Evans, R. Ellison Harding, Paul S. Dick, and Walter Lichtenstein, Secretary.

Mr. Fraser made a statement covering the meeting of the Committee on "Easy Money" Policy of the Council with a committee of the Board of Governors and stated that the spirit of the meeting had been excellent and asked the Secretary of the Council to read the statement which had been agreed upon by both committees, which is as follows:

"The two committees have agreed that the Council does not waive any rights as to publication of its memorandum on the 'easy money' policy, and the Board maintains its right to prepare an answer to the Council's memorandum to be published together with the memorandum of the Council. However, until the Board has prepared and communicated to a committee of the Council a draft of a more comprehensive statement upon which the Board and the Council may agree, the whole question of publication of the Council's memorandum and all matters relative thereto will be left in abeyance."

On motion by Mr. Crosby, seconded by Mr. Dick, it was unanimously voted to state to the Board of Governors that the Council had received the report of its committee and had voted to continue the same committee in the hope that the Board would speedily prepare and communicate to the Committee a preliminary statement of the kind outlined by Chairman Eccles.

The Council approved unanimously the joint statement of the two committees as read by the Secretary of the Council, and it further authorized the President of the Council, in case any member of the committee should be unable to serve, to appoint a substitute for him.

Mr. Steele presented a resolution seeking to arrange for a four-year membership on the Council, reading as follows:

"It was voted unanimously that the Federal Advisory Council recommend to the Conference of Chairmen of the Federal Reserve Banks that it give serious consideration to the adoption by the respective boards of directors of the Banks of a regular plan of rotation among the members of the Federal Advisory Council, such plan to be carried out through voluntary cooperation by the Banks rather than through any change in the statutes. It is the suggestion of the Council that a plan of four year membership on the Council with a consequent change of three members each year be inaugurated. This would give to the Council a sufficient continuity of membership so that its efficiency as a continuing body could be maintained, while at the same time it would permit a sufficient amount of change to insure fresh points of view, prevent too great a crystallization of policies, and avoid the danger of too long continuance in office of any single member."

Mr. Loeb seconded Mr. Steele's resolution, which was unanimously adopted.

The meeting adjourned at 7:10 P. M.

WALTER LICHTENSTEIN,
Secretary

MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

November 19, 1940

At 10:10 A. M. the Federal Advisory Council reconvened in the Board Room of the Federal Reserve Building, Washington, D. C., the President, Mr. Brown, in the Chair.

Present: Mr. Edward E. Brown, President; Mr. Howard A. Loeb, Vice President; Messrs. Thomas M. Steele, Leon Fraser, B. G. Huntington, Robert M. Hanes, Ryburn G. Clay, S. E. Ragland, John Crosby, John Evans, R. Ellison Harding, Paul S. Dick, and Walter Lichtenstein, Secretary.

The Secretary of the Council read the resolution dealing with the suggestion for a regular plan of rotation among the members of the Federal Advisory Council. This appears in the Minutes of the previous day. The resolution was formally adopted.

The Secretary of the Council then read the final form of the resolution providing for a statement by the President of the Council to the press after each meeting of the Council. This resolution appears in the Minutes of the meeting of November 17, 1940. The resolution was formally adopted.

The Secretary of the Council then read the agreement arrived at by the Committee on "Easy Money" of the Council and a special committee of the Board. This resolution appears in the Minutes of the previous day. This resolution was formally adopted.

The meeting adjourned at 10:20 A. M.

WALTER LICHTENSTEIN,
Secretary

MINUTES OF JOINT CONFERENCE OF THE FEDERAL ADVISORY COUNCIL AND THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

November 19, 1940

At 10:30 A. M. a joint conference of the Federal Advisory Council and the Board of Governors of the Federal Reserve System was held in the Board Room of the Federal Reserve Building, Washington, D. C.

Present: Members of the Board of Governors of the Federal Reserve System:

Chairman Marriner S. Eccles; Vice Chairman Ronald Ransom; Governors M. S. Szymczak, John K. McKee, and Ernest G. Draper; also Messrs. Lawrence Clayton, Assistant to the Chairman of the Board of Governors; Elliott Thurston, Special Assistant to the Chairman of the Board of Governors; Chester Morrill, Secretary of the Board of Governors; L. P. Bethea and S. R. Carpenter, Assistant Secretaries of the Board of Governors; Walter Wyatt, General Counsel of the Board of Governors; L. H. Paulger, Chief of the Division of Examinations; E. A. Goldenweiser, Director of the Division of Research and Statistics of the Board of Governors; E. L. Smead, Chief of the Division of Bank Operations of the Board of Governors; and Carl E. Parry, Chief of the Division of Security Loans of the Board of Governors.

Present: Members of the Federal Advisory Council:

Mr. Edward E. Brown, President; Mr. Howard A. Loeb, Vice President; Messrs. Thomas M. Steele, Leon Fraser, B. G. Huntington, Robert M. Hanes, Ryburn G. Clay, S. E. Ragland, John Crosby, John Evans, R. Ellison Harding, Paul S. Dick, and Walter Lichtenstein, Secretary.

There was a lengthy discussion of a letter addressed by the Honorable Jesse H. Jones to the Secretaries of War and Navy which appeared in this morning's newspapers. In this letter Mr. Jones, on behalf of the Reconstruction Finance Corporation, offered to finance plant facility construction contracts at low rates, and under conditions which might possibly make it difficult for private banks to compete with the Government lending agencies. Various members of the Board of Governors stated that they had not had any previous information of this letter, but it was pointed out that possibly the Army and Navy had requested some such action, because these two departments of the Government had at various times insisted that if the payment of contracts were guaranteed by the Government, the maximum rate to be charged for the financing of such contracts should not exceed 1½ per cent.

The President of the Council stated that it would be foolish to jump to conclusions and it might be that Mr. Jones was either not being quoted correctly or that his letter was subject to some other interpretation, but that at the moment it did appear as though the willingness of private institutions to help in the financing would be without avail. Even where the Government guaranteed the payment of a contract, a private institution would always be subject to the danger that a Government department might refuse payment on the ground that not all specifications had been followed. On the other hand, if the Reconstruction Finance Corporation lent money, it really would be one department of the Government lending to another department and therefore the situation would not be at all comparable to the one in which a private lender would find himself.

The President of the Council stated that at a meeting of the Council yesterday evening, the Council had agreed to the statement prepared by the Committee on "Easy Money," representing the Council, and a special committee of the Board. The Secretary of the Council read the agreement, which appears in the Minutes of the previous day.

The President of the Council stated that it was hoped that the two committees would work as rapidly as possible, for some of the members of the Council's committee would not be on the Council next year, and for the sake of continuity it would be desirable to have the work completed while the present members of the Council were still in office.

The President at this point raised the question of the continuity of the Council and asked the Secretary of the Council to read the resolution suggesting a regular plan of rotation among the members of the Federal Advisory Council. This resolution appears in the Minutes of the previous day.

On request, the Secretary of the Council stated that Mr. Steele had moved the adoption of the resolution and his motion had been seconded by Mr. Loeb.

At 11:10 A. M. Governor Chester Davis joined the meeting.

The various members of the Board of Governors stated that they believed the suggestion of the Council was a good one and was an improvement upon the present system.

Chairman Eccles expressed the hope that if the contemplated joint report could not be completed before a new Council took office, that possibly some arrangement might be made for continuing the services of the present members of the Council's committee on that committee until such time as a joint report had been prepared or until it had been decided that it was impossible to reach an agreement on a report.

The Secretary of the Council read the resolution expressing the desire of the Council to have the President of the Council, at the end of each meeting, issue a formal statement to the press. This resolution appears in the Minutes of the meeting of November 17, 1940. There was considerable discussion, but the members of the Board of Governors did not seriously object to the proposed procedure, and in fact thought that it might be well to make some such attempt.

The meeting adjourned at 12:20 P. M.

WALTER LICHTENSTEIN,
Secretary

MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

November 19, 1940

At 12:30 P. M. the Federal Advisory Council reconvened in the Board Room in the Federal Reserve Building, Washington, D. C., the President, Mr. Brown, in the Chair.

Present: Mr. Edward E. Brown, President; Mr. Howard A. Loeb, Vice President; Messrs. Thomas M. Steele, Leon Fraser, B. G. Huntington, Robert M. Hanes, Ryburn G. Clay, S. E. Ragland, John Crosby, John Evans, R. Ellison Harding, Paul S. Dick, and Walter Lichtenstein, Secretary.

The President of the Council suggested that action in the matter of the letter of the Honorable Jesse H. Jones be left to the Executive Committee of the Council.

Mr. Crosby so moved, and this was seconded by Mr. Evans, and the procedure suggested by the President of the Council was unanimously approved.

The President of the Council read the statement which he proposed to release to the press after the adjournment of this meeting, and his statement met with the approval of the members of the Council.

At 12:50 P. M. Mr. Harding left the meeting.

At 12:55 P. M. Mr. Fraser left the meeting.

Discussion continued regarding the letter of Mr. Jones and the general feeling was that if the President of the Council, on further investigation, thought it would be desirable to issue a letter or a statement on the subject, he might do so, and consult in that case with members of the Executive Committee.

The meeting adjourned at 1:10 P. M.

WALTER LICHTENSTEIN,
Secretary

November 18, 1940

Special Committee to Consider Memorandum of
Federal Advisory Council on "Easy Money Policy"

Representing the Board of Governors of the Federal Reserve System: Governors Eccles, Ransom and Szymczak

Representing the Federal Advisory Council: Messrs. Fraser, Loeb, Hanes and Evans

Also present from the Board: Messrs. Morrill, Goldenweiser and Thurston

Also present from the Council: Mr. Lichtenstein

The meeting took place in the Board Room beginning at 3:15 p.m.

Fraser says that there are two questions interrelated in which the Council is interested in connection with the possibility of a joint statement. It is obvious that a joint committee this afternoon cannot get out such a statement. It is, therefore, desirable for the Board to get out a preliminary or first draft to be sent to the members of the Council as soon as possible and then either correspondence can be conducted about this draft or another meeting may be arranged. It is essential that the members of the Council, or the members of the committee of the Council, be shown the preliminary draft so that the memorandum in question will not be a fixed one which the Council would have to take or leave. The Council can then be helpful in the production of a final draft.

Eccles suggests that in case the Board would withdraw its question of April 27, 1940, the Council would withdraw its answer. This is based on the belief that, fundamentally, conditions have changed and there is no point in discussing the question of easy money in a sort of vacuum.

Fraser replies that perhaps there is no need to withdraw either question or answer but, if an agreement were reached on some joint statement covering more or less the same topic, then the question of publication might be waived. This would be especially true if the joint statement contained or included some of the recommendations beginning on page 5 of the Council's memorandum.

Eccles says that, as a matter of record, it would be desirable to have both question and answer withdrawn, for if these are left in the record then there ought to be in the record also an answer by the Board to the Council's memorandum or, in any event, the record ought to show that the Council had revised its answer in such a fashion that the Board would not feel under any necessity of making a further reply.

It was agreed finally that this phase of the matter be postponed, it being understood that in the meantime the Board does not waive its right to file an answer and the Council does not waive its position, but both sides will wait and see what develops.

Evans believes any joint statement must include the essentials of the Council's memorandum, for if present easy money continues, it will be difficult for private industry to function properly.

Eccles says it is obviously the duty of the Board to advise on fiscal and financial policies. The Board is the creature of Congress and is not under any other governmental agency of official such as a cabinet officer. Nevertheless, no central banking system today has an independent status. Of this the Board is conscious and so it occupies a position different from that of the Reserve Banks and private banks. The Board is the connecting link between the Government and the Federal Reserve Banks and the private banking system, and the Board cannot lose sight of its relationship to the Washington picture. It must handle its position carefully without at the same time becoming a mere rubber stamp. Consequently, in speaking of interest rates, it is necessary to watch the emphasis. Rates are not an end in themselves. Some way must be found (1) to deal with excessively easy money, excess reserves, etc., (2) to do financing of deficits outside of the banking system (there is no need of creating more deposits and the Treasury should seek to tap funds outside of the banks), (3) to have a tax system that will tend to bring about a balanced budget so that when there is full employment and full use of productive capacity, deficit financing will disappear, and (4) to avoid bottlenecks. If reference is made merely to the one item of interest rates, it would appear as if banks were the only consideration in the picture and that no attention was being given to the much broader problems. Not merely the monetary question must be considered, but also the fiscal situation and, on the other hand, direct control of bottlenecks, etc., must also be considered.

Loeb points out that possibly on some points the Council ~~goes further than the Board.~~ may desire to go further or not as far as the Board.

Eccles says that this would depend on what the points are but the Council is not necessarily limited by the action of the Board.

The Board felt that the memorandum on "Easy Money" put the Board in an unfair light and did not tell the whole story. For example, there wasn't any distinction made between the Board and the Administration. However, the Council's right to express its point of view is not at all being questioned.

Fraser points out that if money is too cheap it will not be possible to interest private investors in Government securities. The banking system feels that the Board, even now, has not made any statement as is being contemplated here, now that conditions have changed and easy money is not helpful.

Eccles says that since 1938 easy money has not been an aid in the situation and he claims to have made speeches to this effect.

Ransom feels that the Council in its memorandum has overemphasized what the Board has said and has paid little attention to what the Board has really done.

Eccles says that he made a speech in St. Louis dealing with this whole question but that he had to bring in the tax problem for, after all, interest rates are not something that operate in a vacuum.

When reserve rates were raised, bankers criticized severely. How many bankers are there who would be willing to have the tax program, reserves, gold and silver dealt with as they should be?

Fraser repeats that there isn't a banker in the country who would object to the sterilization of gold or some other effective method.

Szymczak wants to know what the banking attitude would be if the Board asked for more power to limit excess reserves.

Evans replies that the trouble is it would not be an automatic function.

Eccles says that all he asked in 1935 was the power to limit excess reserves to $500,000,000 or $1,000,000,000. In other words, there would have been an automatic point. Today he questions whether it is desirable to have the control rigid or entirely automatic because it is too difficult to see ahead.

Evans says Eccles did not sell his ideas in 1935 and bankers felt that Eccles wanted power to give him unlimited control over reserves and that, therefore, the banker from day to day did not know what lending policy to adopt.

Ransom points out that under present conditions the Treasury can neutralize any action of the Board by the authority given it under the Thomas Amendment and the Act creating the stabilization fund. The question is whether the Federal Reserve System is or is not a central bank.

Eccles feels that, in spite of the Treasury, the stabilization fund did not play much of a role as, after all, it involves only $2,000,000,000. The Thomas Amendment and the Silver Purchase Act should be repealed. There is great need of cooperation between the Treasury and the System as regards fiscal policy. In the face of deficits, a central bank cannot be too independent.

Fraser says that there is substantial agreement that if we should be drawn into the war, either in the East or in the West, we must be prepared fiscally and financially just as much as we must be in respect to armaments. He agrees with Evans that bankers are afraid to give a few people complete power to manage reserves for the powers might be used to accomplish results which have little or nothing to do with financial and fiscal policies.

Eccles admits that there is real basis for such fears and says the Board hesitated to lower reserves in 1938. He points out that the Council apparently approved the action of the Board at the time and that in practice it really did not change the situation.

Ransom agrees that, in light of everything, the decision to reduce reserve requirements in 1938 was a wise one.

Fraser read recommendations made by the Council beginning on page 5 of the memorandum and inquires whether there is any objection to any of these recommendations.

Eccles states that he would be willing to go even further if the whole statement is put in the right perspective. Since 1938, easy money has not been needed but interest rates must be placed in the right framework if the report is to be effective. The Board's portfolio is being reduced but, in light of occurrences of the last two or three weeks, it is very fortunate that the System did not run out of ammunition earlier. This ammunition must be conserved and the portfolio must not be allowed to run down to the subsistent point. Eccles would not hesitate to explain to a committee of Congress many questions which it would be difficult to raise in a statement.

Ransom read a prepared statement of objectives, as follows:

1. Avoid bottlenecks.
2. Prevent a collapse when defense program is finished.
3. Deal with excess reserves.
4. Do not increase deposits by having banks buy more bonds.
5. Balance the budget.
6. Have a tax program to help bring about these objectives.

Eccles points out that one of the things that ought to be discussed is the need of more unification in the banking system for, at present, 60 per cent of the banks are not in the System and it is relatively easy for any member of the System to get out of the System so that banks might feel that, if reserve requirements were increased too much, it would be more profitable not to remain in the System.

Loeb suggests that the Federal Deposit Insurance Corporation Act might be amended so as to make the Federal Reserve System more effective, but Eccles and Ransom objected to giving the Federal Deposit Insurance Corporation power over reserves.

Eccles repeats that it will be necessary to discuss excess reserves and probably the causes of excess reserves must be discussed. He doesn't know whether the Board would be willing to go so far as to indicate that the further acquisition of gold might be checked, but an amendment of the Johnson Act permitting Great Britain to borrow on securities might be mentioned. The question is whether possibly direct grants should be made. It might be put in such a way that reference need not be made directly to Great Britain but rather to permit an agency of any nation whose cause we are supporting to use its assets as collateral for advances. Also, instead of leasing naval and air bases, why couldn't we buy outright those that are apparently needed for our defense purposes?

Fraser suggests that as gold came in, required reserves might be increased on this additional gold to the same amount as the gold coming in.

Eccles points out that excess reserves are not evenly distributed throughout the country and there are parts of the country where loans have increased without much increase in deposits. The question of excess reserves is really a problem of the money market and there cannot be a blanket regulation. New York has $3,000,000,000 of the excess reserves and an increase in reserve requirements might well be applied to the money market loan. This would make it easier to reverse the action if the situation should change and the Board or the Reserve Banks would have to consult the money market. He claims he is not opposed to interbank deposits. He has been for a unified banking system so as to have better monetary control. He believes that deposit insurance charged on reserves carried in the Federal Reserve Banks should be discontinued. It seems ridiculous to charge insurance on funds that are locked up. It is impossible to treat of the interest rate structure without dealing with some of these other matters to which reference has been made. He would like to see a statute increasing required reserves of all banks, not merely of member banks.

In this connection Mr. Lichtenstein read a statement embodying what he understood to be the agreement of the two committees, reading as follows:

> "The two committees have agreed that the Council does not waive any rights as to publication of its memorandum on the 'easy money' policy, and the Board maintains its right to prepare an answer to the Council's memorandum to be published together with the memorandum of the Council. However, until the Board has prepared and communicated to a committee of the Council a draft of a more comprehensive statement upon which the Board and the Council may agree, the whole question of publication of the Council's memorandum and all matters relative thereto will be left in abeyance."

Both committees expressed their agreement with the statement as read.

For Release in Morning Papers of
Tuesday, November 19, 1940

FLA-60

FEDERAL LOAN AGENCY

WASHINGTON

November 18, 1940.

JESSE JONES, FEDERAL LOAN ADMINISTRATOR, TODAY MADE PUBLIC THE ATTACHED LETTER WHICH WAS SENT INDIVIDUALLY TO THE SECRETARY OF WAR AND THE SECRETARY OF THE NAVY:

FEDERAL LOAN AGENCY

WASHINGTON

November 18, 1940

Dear Mr. Secretary:

You may recall that Congress increased the borrowing authority of the RFC by $1,000,000,000 to enable it to assist in the defense program - plant construction, et cetera - and, while substantial commitments have already been made, ample funds are still available, and the Corporation wants to continue to be helpful wherever it can.

It is desirable that banks finance as much of the defense program as they can handle properly, but where credit is extended upon a definite agreement for reimbursement by the War or Navy Department, the interest rate should bear some relation to a government guaranteed obligation.

I am writing to advise that where, in accordance with your established policy, there is a definite undertaking on the part of the War or Navy Department, in a manner mutually acceptable, for reimbursement over a period of five years, the RFC, either directly or through banks or the Defense Plant Corporation, will arrange or adjust such financing at an interest rate of 1½% per annum on payments made within the period.

For defense financing, for working capital and plant equipment and expansion, where there is no definite undertaking for reimbursement by the War or Navy Department, the interest rate will be appropriate to the credit factors of the individual case, but not more than 4%.

Sincerely yours,

(Signed) Jesse H. Jones

Administrator

FEDERAL ADVISORY COUNCIL

Statement for the Press

For immediate release November 19, 1940.

Edward E. Brown, the president of the Federal Advisory Council, stated today that the Council had concluded its regular quarterly three-day meeting with all its members present from each of the twelve Federal Reserve Districts.

The Council met twice with the Board of Governors of the Federal Reserve System, in addition to holding several sessions of its own. Various matters affecting the Federal Reserve System were considered. Much time was given to discussions of ways and means by which the largest possible participation of the banks of the country and private capital could be obtained in connection with the financing of the defense program. The Council reported that the banks of the country were anxious to participate to the fullest possible extent consistent with sound banking and both the Board of Governors of the Federal Reserve System and the Council were in agreement that as much of the financing as possible should be done by the banking system.

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SPECIAL REPORT TO THE CONGRESS
by
the Board of Governors of the Federal Reserve System,
the Presidents of the Federal Reserve Banks,
and the Federal Advisory Council

For the first time since the creation of the Federal Reserve System, the Board of Governors, the Presidents of the twelve Federal Reserve Banks, and the members of the Federal Advisory Council representing the twelve Federal Reserve Districts present a joint report to the Congress.

This step is taken in order to draw attention to the need of proper preparedness in our monetary organization at a time when the country is engaged in a great defense program that requires the coordinated effort of the entire Nation. Defense is not exclusively a military undertaking, but involves economic and financial effectiveness as well. The volume of physical production is now greater than ever before and under the stimulus of the defense program is certain to rise to still higher levels. Vast expenditures of the military program and their financing create additional problems in the monetary field which make it necessary to review our existing monetary machinery and to place ourselves in a position to take measures, when necessary, to forestall the development of inflationary tendencies attributable to defects in the machinery of credit control. These tendencies, if unchecked, would produce a rise of prices, would retard the national effort for defense and greatly increase its cost, and would aggravate the situation which may result when the needs of defense, now a stimulus, later absorb less of our economic productivity. While inflation cannot be controlled by monetary measures alone, the present extraordinary situation demands that adequate means be provided to combat the dangers of overexpansion of bank credit due to monetary causes.

The volume of demand deposits and currency is fifty per cent greater than in any other period in our history. Excess reserves are huge and are increasing. They provide a base for more than doubling the existing supply of bank credit. Since the early part of 1934 fourteen billion dollars of gold, the principal cause of excess reserves, has flowed into the country, and the stream of incoming gold is continuing. The necessarily large defense program of the Government will have still further expansive effects. Government securities have become the chief asset of the banking system, and purchases by banks have created additional deposits. Because of the excess reserves, interest rates have fallen to unprecedentedly low levels. Some of them are well below the reasonable requirements of an easy money policy, and are raising serious, long-term problems for the future well-being of our charitable and educational institutions, for the holders of insurance policies and savings bank accounts, and for the national economy as a whole.

The Federal Reserve System finds itself in the position of being unable effectively to discharge all of its responsibilities. While the Congress has not deprived the System of responsibilities or of powers, but in fact has granted it new powers, nevertheless, due to extraordinary world conditions, its authority is now inadequate to cope with the present and potential excess reserve problem. The Federal Reserve System, therefore, submits for the consideration of the Congress the following five-point program:

1. Congress should provide means for absorbing a large part of existing excess reserves, which amount to seven billion dollars, as well as such additions to these reserves as may occur. Specifically, it is recommended that Congress -

(a) Increase the statutory reserve requirements for demand deposits in banks in central reserve cities to 26%; for demand deposits in banks in reserve cities to 20%; for demand deposits in country banks to 14%; and for time deposits in all banks to 6%.

(b) Empower the Federal Open Market Committee to make further increases of reserve requirements sufficient to absorb excess reserves, subject to the limitation that reserve requirements shall not be increased to more than double the respective percentages specified in paragraph (a).
(The power to change reserve requirements, now vested in the Board of Governors, and the control of open market operations, now vested in the Federal Open Market Committee, should be placed in the same body.)

(c) Authorize the Federal Open Market Committee to change reserve requirements for central reserve city banks, or for reserve city banks, or for country banks, or for any combination of these three classes.

(d) Make reserve requirements applicable to all banks receiving demand deposits regardless of whether or not they are members of the Federal Reserve System.

(e) Exempt reserves required under paragraphs (a), (b) and (d) from the assessments of the Federal Deposit Insurance Corporation.

2. Various sources of potential increases in excess reserves should be removed. These include: the power to issue three billions of

greenbacks; further monetization of foreign silver; the power to issue silver certificates against the seigniorage, now amounting to one and a half billion dollars on previous purchases of silver. In view of the completely changed international situation during the past year, the power further to devalue the dollar in terms of gold is no longer necessary or desirable and should be permitted to lapse. If it should be necessary to use the stabilization fund in any manner which would affect excess reserves of banks of this country, it would be advisable if it were done only after consultation with the Federal Open Market Committee whose responsibility it would be to fix reserve requirements.

3. Without interfering with any assistance that this Government may wish to extend to friendly nations, means should be found to prevent further growth in excess reserves and in deposits arising from future gold acquisitions. Such acquisitions should be insulated from the credit system and, once insulated, it would be advisable if they were not restored to the credit system except after consultation with the Federal Open Market Committee.

4. The financing of both the ordinary requirements of Government and the extraordinary needs of the defense program should be accomplished by drawing upon the existing large volume of deposits rather than by creating additional deposits through bank purchases of Government securities. We are in accord with the view that the general debt limit should be raised; that the special limitations on defense financing should be removed; and that the Treasury should be authorized to issue any type of

securities (including fully taxable securities) which would be especially suitable for investors other than commercial banks. This is clearly desirable for monetary as well as fiscal reasons.

5. As the national income increases a larger and larger portion of the defense expenses should be met by tax revenues rather than by borrowing. Whatever the point may be at which the budget should be balanced, there cannot be any question that whenever the country approaches a condition of full utilization of its economic capacity, with appropriate consideration of both employment and production, the budget should be balanced. This will be essential if monetary responsibility is to be discharged effectively.

In making these five recommendations, the Federal Reserve System has addressed itself primarily to the monetary aspects of the situation. These monetary measures are necessary, but there are protective steps, equally or more important, that should be taken in other fields, such as prevention of industrial and labor bottlenecks, and pursuance of a tax policy appropriate to the defense program and to our monetary and fiscal needs.

It is vital to the success of these measures that there be unity of policy and full coordination of action by the various Governmental bodies. A monetary system divided against itself cannot stand securely. In the period that lies ahead a secure monetary system is essential to the success of the defense program and constitutes an indispensable bulwark of the Nation.