MINUTES OF MEETING
of the
FEDERAL ADVISORY COUNCIL
September 19-20, 1943
and of the
MONTHLY MEETING
of the
EXECUTIVE COMMITTEE
October 6, 1943

MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

September 19, 1943

The third statutory meeting of the Federal Advisory Council for 1943 was convened in Room 336 of the Mayflower Hotel, Washington, D. C., on Sunday, September 19, 1943, at 2:00 P. M., the President, Mr. Brown, in the chair.

Present:

Mr. George L. Harrison	District No. 2
Mr. William Fulton Kurtz	District No. 3
Mr. B. G. Huntington	District No. 4
Mr. Robert V. Fleming	District No. 5
Mr. H. Lane Young	District No. 6
Mr. Edward E. Brown	District No. 7
Mr. Ralph C. Gifford	District No. 8
Mr. Lyman E. Wakefield	District No. 9
Mr. W. Dale Clark	District No. 10
Lt. Col. Jay L. Taylor (Alternate for Mr. Nathan Adams)	District No. 11
Mr. George M. Wallace	District No. 12
Mr. Walter Lichtenstein	Secretary

Absent:

Mr. Charles E. Spencer, Jr.	District No. 1

The Secretary of the Council stated that Mr. Spencer was unable to be present and that no alternate had been appointed for him; also, Mr. Adams would not be present, but Lieutenant Colonel Jay L. Taylor, Deputy Director, Fuels and Lubricant Division, Quartermaster General, would serve as alternate for Mr. Adams.

On motion, duly made and seconded, the minutes of the Council meetings of February 14-15, 1943, and May 23-24, 1943, and of the Executive Committee meetings of January 6, 1943, and April 7, 1943, copies of which had been previously sent to the members, were approved.

The President of the Council asked informally whether the banks represented on the Council had had a request from the SEC to analyze approximately two hundred accounts of executives of large corporations. In Chicago, a number of the banks had been approached, but had informed the SEC that such a request should be made either through the Comptroller of the Currency or through the regional Federal Reserve bank.

The first topic to be considered was the competition with private business of governmental agencies. It was decided to point out to the Board of Governors the threat involved to the independent banker by the activities of such agencies as the Production Credit Administration and the Commodity Credit Corporation and to ask the Board to support the Wherry Bill (S914) and the Butler proposal (Senate Concurrent Resolution 8).

There was a short discussion about the expenses to banks arising out of bond drives, but it was decided not to approach the Board of Governors in regard to the subject.

A lengthy discussion took place in respect to the situation created by the cancellation of war contracts and especially the difficulties of subcontractors.

On page 817 of the September number of the *Federal Reserve Bulletin* a ruling appeared in respect to Regulation Q.

It was decided to ask the Board of Governors what further steps it was planning to take.

Consideration was given to the various plans dealing with international monetary stabilization. On motion of Mr. Fleming, seconded by Mr. Wakefield, it was voted unanimously to ask the Executive Committee of the Council, at its meeting on October 6 to consider the desirability of presenting a formal memorandum to the Board of Governors on this subject.

The meeting adjourned at 5:15 P. M.

WALTER LICHTENSTEIN,
Secretary.

MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

September 20, 1943

At 10:00 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. George L. Harrison, Vice President; Messrs. William Fulton Kurtz, B. G. Huntington, Robert V. Fleming, H. Lane Young, Ralph C. Gifford, Lyman E. Wakefield, W. Dale Clark, George M. Wallace, and Walter Lichtenstein, Secretary.

A short discussion took place in respect to the various matters agreed upon at the meeting held yesterday.

The meeting adjourned at 10:50 A. M.

WALTER LICHTENSTEIN,
Secretary.

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

September 20, 1943

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:

Vice Chairman Ronald Ransom; Governors John K. McKee, Ernest G. Draper, and R. M. Evans; also Messrs. Lawrence Clayton, Assistant to the Chairman; Chester Morrill, Secretary of the Board of Governors; Liston P. Bethea and S. R. Carpenter, Assistant Secretaries to the Board of Governors; Walter Wyatt, General Counsel; J. P. Dreibelbis, General Attorney; Leo H. Paulger, Chief, Division of Examination; Edward L. Smead, Chief, Division of Bank Operations, and Carl E. Parry, Chief, Division of Security Loans.

Present: Members of the Federal Advisory Council:

Mr. Edward E. Brown, President; Mr. George L. Harrison, Vice President; Messrs. William Fulton Kurtz, B. G. Huntington, Robert V. Fleming, H. Lane Young, Ralph C. Gifford, Lyman E. Wakefield, W. Dale Clark, George M. Wallace, and Walter Lichtenstein, Secretary.

The President of the Council discussed the competition with private business of governmental lending agencies and pointed out, that in the opinion of the Council, the System has a real interest in the situation for small banks are withdrawing from the System in order to be able to impose exchange charges and thus continue to exist. The President of the Council expressed the hope that the Board will use its influence in Congress to point out the dangers of the present situation, and he made special reference to Senate Bill 914, introduced by Senator Wherry, and the Senate Concurrent Resolution 8, introduced by Senator Butler.

The President of the Council discussed the problem of terminal loans and the seriousness of the whole situation to banks involved in the cancellation of contracts. If a breakdown of industry and the banking system is to be avoided, it will be necessary to provide some form of automatic advances without awaiting the result of detailed audits. It is hoped that the Board is keeping in close touch with developments.

After some statements by members of the Board of Governors, the President of the Council expressed himself as being satisfied with the attitude of the Board and convinced that the Board is trying to keep abreast of the situation.

In respect to Regulation Q, Governor McKee stated the opinion in the September number of the *Federal Reserve Bulletin* would now be a guide for all bank examiners and that if a bank fails to comply with the ruling established, the Comptroller of the Currency or one of the other supervising agencies should take further action.

The President of the Council discussed international monetary stabilization and pointed out that it was evident that members of the Federal Advisory Council were unanimous in their opposition to all the plans so far presented. He stated the Council had asked its Executive Committee to draw up a memorandum at the appropriate time and to submit such directly or through the Board to the Treasury. The Council believed the way to proceed was to bring about a pound sterling-dollar stabilization in which would be included the Canadian dollar.

The President of the Council discussed the inquiry made by the SEC which he had brought to the attention of the members of the Council at the meeting yesterday. It was stated that the Board of Governors had never heard of this action of the SEC but would make inquiry in respect to it.

The meeting adjourned at 1:15 P. M.

WALTER LICHTENSTEIN,
Secretary.

MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

September 20, 1943

At 2:30 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. George L. Harrison, Vice President; Messrs. William Fulton Kurtz, B. G. Huntington, Robert V. Fleming, H. Lane Young, Ralph C. Gifford, Lyman E. Wakefield, George M. Wallace, and Walter Lichtenstein, Secretary.

Dr. E. A. Goldenweiser, Director of the Division of Research and Statistics, appeared before the Council and discussed the present and post-war industrial situation, especially the problem of inflation and deflation. In his opinion, the most serious problem which will have to be solved is that of possible unemployment after the war.

Dr. Goldenweiser also discussed briefly the stabilization plans.

The meeting adjourned at 3:45 P. M.

WALTER LICHTENSTEIN,
Secretary.

NOTE: This transcript of the Secretary's notes is not to be regarded as complete or necessarily accurate. The transcript should be considered as being strictly for the sole use of the members of the Federal Advisory Council.

W. L.

Secretary's notes on meeting of the Federal Advisory Council on September 19, 1943, at 2:00 P. M. in Room 336 of the Mayflower Hotel, Washington, D. C.

Messrs. Spencer and Adams were not present, but Lt. Col. Jay L. Taylor, Deputy Director, Fuels and Lubricant Division, Quartermaster General, acted as alternate for Mr. Adams. The other members of the Council were all present as also the Secretary of the Council. Mr. Kurtz was not present at the beginning of the meeting but joined it at 2:20 P. M.

The minutes of the meeting of May 23-24 which had been previously sent to all the members of the Council were approved.

Brown asked informally whether the banks represented on the Council had had a request from the SEC to analyze two hundred or so accounts of executives of large corporations. In Chicago a number of the banks had been approached but had informed the SEC that such a request ought to come either through the Comptroller or through the Federal Reserve Bank.

It was decided to leave the discussion of the first topic on the agenda to the last.

COMPETITION OF GOVERNMENTAL AGENCIES

Young states the most serious problem at the moment is the competition of the Production Credit Administration. He believes if carried far enough another banking fiasco could be created. He did not think the Legislative Committee of the American Bankers Association had handled the matter very satisfactorily, but the resolution passed at the recent convention in New York was entirely satisfactory. This resolution asks for an investigation and study of PCA alone as being the most important competitor of commercial banks at the moment. He suggests asking the Board of Governors to back up in Congress the request of the A. B. A. to have an investigation of this agency and says that as a result of the activity of the PCA, the Federal Reserve System is losing members.

Brown says the Commodity Credit Corporation, as far as dollar volume is concerned, is just as important as the P. C. A.

Young agrees, but says that while the CCC affects the larger banks more, the PCA is especially important for the country banks.

Brown admits that as a matter of tactics, it may be well to attack the PCA first, though all these governmental lending agencies are more or less on the same basis.

Fleming says the other side of the picture is that some of the small banks have been charging too much.

Taylor. There is another factor which must be considered. Bankers were not willing to make an annual loan or one for 13 months, which is what is needed by sheep raisers and often the borrower found difficulties being made when he wanted to renew the loan. In other words, bankers at one time were not willing to make loans for sufficiently long terms.

Young answers that this practice is entirely changed and that bankers are now making loans to cover the period needed to market the product.

Taylor tells of an agency in Texas of which he is vice president. This agency was formed in order to make credit available when sufficient credit from banks was not to be had. The agency at present is quite ready to wind up its business, but it wants to be certain that credit will be available in bad times as well as good.

Harrison believes the situation can be met by having a provision in the law that a Government agency can only lend in those instances where credit at fair rates cannot be obtained from the usual private and commercial lending agencies.

Brown states that all that should be asked is that the Government should not subsidize agencies for the main purpose of competing with private capital.

Wakefield points out that all this is a part of the attempts to socialize all credit agencies.

Brown states that he will point out to the Board the threat involved to the independent banker and that the Council recommends to the Board that it support the Wherry Bill (S.914) and the Butler proposal (Senate Concurrent Resolution 8) to investigate the situation. He believes such an investigation would reveal that competition with banks is being financed by the Government in cases where banks are amply able to take care of legitimate credit demands.

Fleming thinks the investigation ought also to look into the present system of governmental guarantees.

Brown adds to his previous statement that he will call the attention of the Board to the fact that as a result of the competition by the Government, many small banks are withdrawing from the System in order that they may be able to live by making exchange and other service charges.

TREASURY SHOULD ASSUME EXPENSES OF BOND DRIVES

Kurtz said banks were affronted by the Treasury asking them to finance all the bond drives. In Pennsylvania the Treasury asked the banks to contribute $30 thousand and received only $10 thousand. He feels this is destroying the morale in connection with bond drives.

Brown and Fleming point out that the Federal Reserve Banks cannot do anything about this matter.

Wallace says to make this demand at this time would be bad timing.

Brown says the worst thing banks could do at this time would be to raise the question of expense as it would arouse great antagonism in the Treasury and in the Administration as a whole against the banks. He feels that any charge made by banks at this time would be very much resented.

Wakefield not willing to argue with the Treasury about this matter as it would certainly be used ultimately against the banks.

Kurtz does not want banks to charge anything, but believes the present situation is hurting the morale of the small banks and he thinks the Treasury ought to make some appropriation to reimburse banks, especially small banks.

It was agreed not to discuss this matter with the Board of Governors, but members of the Council might find it possible to discuss the subject informally with Messrs. Morgenthau and Bell.

CANCELLATION OF WAR CONTRACTS

Kurtz suggested withdrawing this topic but Brown says that it might be well to discuss the situation. He believes something more than VT loans is needed and there ought to be some sort of T loan not covered by the VT loans. The War Department is quite right in refusing to deal with anyone except the principal contractor for it would be extremely difficult for the War Department or any other one of the departments to deal with the vast multitude of subcontractors. The War Department has been considering this whole subject but no conclusion has been reached. The Murray Bill provides that 80 per cent of the claims of subcontractors be settled by Government advances. Another thought is to advance 80 or 90 per cent of the value of tools, machinery, and the like which has been used purely for the purpose of war work. Another proposal is to have a termination loan by which the bank would lend say 80 per cent of whatever the claim might be and the bank would thereby take a substantial part of the risk, so that if the claim were overstated by 20 per cent the bank would lose. For the unguaranteed part of the loan, the bank might be permitted to charge 4-5 per cent. After all, the banks are the only ones who would be familiar with the subcontractor's situation.

Kurtz says that if there were some form of affidavit, then perhaps some paper could be devised which could be made assignable and could be used as a sort of collateral, especially if there is a Government guarantee of 80 per cent of the claim attached.

Wakefield believes it would be dangerous for banks to refuse to assume any part of the risk.

Brown is willing to assume a fair share of the risk on T loans and this would cover subcontractors as well as the chief contractor. There is a danger that some small banks might assume too much of the risk.

Kurtz feels the percentage of guarantee on a T loan should be higher than in the case of a V or VT loan.

Brown says he would rather have the higher interest than the higher guarantee while Wallace wants a lower rate and higher guarantee.

Brown wants to find out whether the Services are considering a T loan with a higher interest rate where the bank assumes a substantial part of the risk. Manufacturers have preferred advances from the Ordnance Department but, of course, these would not cover subcontractors.

Kurtz says the small contractor is the one who has not been taken care of. For one thing, he doesn't know as a rule how to go about getting a V or a VT loan.

Brown believes the guarantee should be solely for the purpose of liquidating war contracts and also such guarantees should cease as soon as the war business is wound up. Otherwise, we'll have the Government permanently in the business of guaranteeing loans which would ultimately undermine the banking business.

Kurtz is afraid that if the settlement is left to the principal contractor, he may put the screws on the subcontractor in order to obtain a more favorable settlement of the claims against him in the event the subcontractor is desperately in need of funds. He believes the chief contractor should be required to settle at once with the small subcontractors in case of any kind of terminal loan.

Brown points out there are many subcontractors who work for a large number of different principal contractors.

Fleming says he believes a certification from the prime contractor as to the subcontractor should be required.

REGULATION Q

Brown discusses the opinion on violation of Regulation Q which appeared on page 817 of the September Federal Reserve Bulletin.

Fleming is curious to know whether the matter is to be considered ended with the mere rendering of an opinion, or whether the Board intends to take any further steps.

INTERNATIONAL CURRENCY STABILIZATION

Harrison raises the question whether the Council ought to take any position. He feels the plans presented are not satisfactory. The way to begin is not by a global arrangement but by regulating the pound sterling dollar exchange.

Wakefield discusses the Chicago Conference.

Huntington presents the following letter from Mr. Leon Fraser, President of the First National Bank of New York, dated September 14, 1943:

> "As at present advised, I am not in favor of the White plan, and certainly not in favor of the Keynes plan which I regard as something of an ingenious joke.
>
> "The four principal reasons for not falling in with the White plan are, first, that it is premature and that plans of this kind are subsequent rather than first steps. It is also a political bank and a debtor bank. Considerable preparatory work must be done before anything so world-wide as the White plan can hope to succeed. In the second place, I feel it is preferable to separate the transition problems from the permanent problems, and this is clearly indicated in your own letter. In the third place, I feel that instead of scrapping all the existing machinery we should build on what we have - with modifications, of course. This includes using the Import-Export Bank, the Bank for International Settlements, 'V' loans to help international trade, the Stabilization Fund, Central Bank cooperation, and all the rest. In the fourth place, the White plan does not tell us the whole story. It says that it is but one of the many steps that should be taken without telling us the other steps and how much they are going to cost the United States. It seems to me that we are entitled to have the whole package or at least a skeleton sketch of it before being asked to accept one segment.

"Furthermore, I feel the general approach is wrong and that instead of a global, grandiose institution from which wonders will be expected, we ought to deal frankly and honestly with the British situation, which is one though not the only outstanding financial problem. A fault of White's plan, and to a greater degree of Keynes' plan, is that they try to camouflage the British difficulty and merge it into a world situation. I believe that it should be tackled directly and that we should help - particularly in dealing with the blocked sterling balances which run into the equivalent of billions of dollars. Few things would start world trade and finance more quickly back on normal lines than the release to their owners of the huge volume of blocked funds held in London and New York. We have plenty of resources to pay off our own and I believe we should make a long term loan to the British to permit them to make London a free market once more.

"I agree with you that a long term lending institution should be totally separate from any stabilization institution or clearing arrangement. I am not convinced that a universal clearing arrangement is necessary. If, through mutual aid, we could get the dollar-sterling rate settled, and if we were prepared to make long term loans to needy areas, it seems to me that a good deal of the clearing would then become automatic. It is not to be forgotten that countries other than the United States today hold more gold, valued in dollars, than was held by the entire world, including the United States, in 1929. It is not to be forgotten that all of South America has more gold and more dollars than at any time in their history and that the same is true of the neutral countries - Portugal, Sweden, and Switzerland. It is also not to be forgotten that many of the countries under the heel of the Nazis are very rich in external assets - notably France, Holland, and Belgium. Spain is in better shape than she has been for a quarter of a century. So I am convinced that as a practical matter, if we continue Lend-Lease to the devastated areas in the transition period and give credits to Great Britain, China, and perhaps to our perennial borrowers in the Balkans, things may get themselves adjusted, providing we keep our own house in order. I agree heartily with the report of the Policy Committee of the A. B. A. which covers the White plan, and I was privileged to cooperate in its preparation.

"Put otherwise, I approach the subject from a realistic point of view, namely, that as practically the only creditor nation we should not hide our light under the bushel of a new international bank and pretend that it is doing the lending and, by the same token, I would deal with the British problem first and by itself. This does not mean that an international institution such as a greatly modified B. I. S. cannot be of infinite use, and I feel that we should use it from the beginning primarily as a meeting place for consultation, planning, exchange of information, and relatively modest short term seasonal credits.

"While I agree, therefore, with your letter in its fundamental aspects, I am still not certain that trade clearing agreements are going to be necessary except, perhaps, for the transition period. Certainly we should try to get away from them because they always lead to bilateral arrangements and quota systems and these always reduce the aggregate of world trade."

Brown feels the Council should tell the Board that conferences of the nature held in Chicago are all to the good. It is obvious there isn't any settled opinion in this country. The Council is opposed to the idea of the Keynes, White, and Canadian plans. On the basis of present information the Council feels any stabilization plan should wait until countries are rehabilitated and internal situations are stabilized. A better approach would be one of temporary stabilization at least between the dollar and the pound sterling, and in this should be included the Canadian dollar which has such great importance for us.

Wakefield calls attention to the unknown attitude of Russia which might wreck any plan. If we could make an arrangement with Great Britain, this would stabilize a very high percentage of international trade.

Brown continues summarizing the sense of the meeting. He advises against any formal memorandum at this time though it might be a good idea to ask the Board when it would be desirable to have the Council present a memorandum.

Harrison suggests a committee of the Council be appointed to study the question and to begin to prepare a memorandum.

It is moved by Fleming and seconded by Wakefield that a committee be appointed along the lines suggested by Mr. Harrison.

Harrison suggests that the whole problem should be left to the Executive Committee which is to meet on October 6, and it was so voted.

The meeting adjourned at 5:15 P. M.

The Council met in the Board Room of the Federal Reserve Building at 10:00 A. M. on September 20, 1943.

Messrs. Spencer and Adams, and Lieutenant Colonel Taylor, alternate for Mr. Adams, were not present.

There was a very short discussion of the various matters agreed upon yesterday.

The meeting adjourned at 10:50 A. M.

At 10:30 A. M. the Council held a joint meeting with the Board of Governors of the Federal Reserve System.

All members of the Council, except Messrs. Spencer and Adams, were present and the following members from the Board of Governors: Governors Ransom, McKee, Draper, and Evans; also Messrs. Morrill, Carpenter, Bethea, Clayton, Wyatt, Dreibelbis, Paulger, Smead, and Parry.

COMPETITION OF GOVERNMENTAL LENDING AGENCIES.

Brown. At the time when established banks were not able to take care of the needs of agriculture governmental agencies were necessary, but at present they create a serious situation for the small country banks whose loans are being taken away by these concerns subsidized with the taxpayers' money. He hopes the Board will support the bill pending in Congress asking for an investigation of these agencies. The System has a real interest in this situation for small banks are withdrawing from the System in order to be able to impose exchange charges and thus continue to exist. The Atlantic District and similar districts are affected most by the PCA, but the CCC is of greater importance in the Chicago and some other districts.

Young. Agriculture in the Sixth District and especially in Georgia consists largely of small farms. Originally, PCA was to be a standby organization for emergencies, but now it is competing vigorously on a permanent basis. It is true that at one time small country banks were charging too much, but now their charges are not excessive. Country banks at present can not get any loans and many depend almost entirely on service charges. Country banks would charge about 5-6 per cent.

McKee says the simplest way to adjust the situation would be to get a law through Congress which would compel all governmental lending agencies to be like the Federal Reserve Banks under section 13 b, that is, to be allowed to extend credit only if credit can not be obtained through regular commercial channels.

Young says one of the troubles is that salesmen acting for the PCA make out a tentative program for a prospective borrower on terms which it would be impossible for a bank to accept, but when the loan is actually to be made the program is revamped and conditions imposed under which a bank could also have functioned.

Brown states the attitude of the RFC and the Federal Reserve System in making loans has been very different. He hopes the Board will use its influence in Congress to point out the dangers in the present situation. He makes reference especially to Senate Bill 914, introduced by Senator Wherry and the Senate Concurrent Resolution 8, introduced by Senator Butler.

Evans. He said the Board had received complaints about the RACC and in consequence the Board induced the RACC to instruct its people not to solicit loans except when credit could not be obtained in the usual way. This has had a good effect. It is evident some of the other agencies will have to be restrained. He believes farmers are willing to pay private banking agencies somewhat more than the governmental agencies. Bankers must make certain that their position is one which the farm block can not criticize successfully. It will probably not be possible to get rid of these governmental agencies but it may be possible to restrain their activities, and PCA is able to underbid private agencies because it has the capital of $120,000,000 from the Government.

Clark agrees with Lane Young. He read statistics to show how many of the chattel mortgages in Nebraska are held by Government agencies.

Wallace says California banks are affected. Banks in California would like to go further than just attack PCA as they object to many of the other agencies, but perhaps it may be wiser to take up one agency at a time.

Ransom says this whole business of Government loans and guarantees is a most serious threat to private banking, but it is not realistic to think this can be stopped suddenly. It will require much effort to bring about a change. The Federal Reserve Board is somewhat puzzled by the existing maze which is constantly growing worse. He believes the new president of the ABA is an excellent selection in view of this situation as he is thoroughly familiar with it.

TERMINAL LOANS

Brown asks as to the study the Board must be making of this whole subject. The Council realizes this is more a concern of the armed services than of the Board of Governors of the Federal Reserve System. At the moment, there is a discussion going on in Chicago in a meeting called by the Ordnance Department. There have been various suggestions made such as that banks should be guaranteed for a certain percentage of a loan and a lower rate of interest should be charged on the guaranteed part of the loan than on the unguaranteed part. The Ordnance Department quite naturally wishes to deal with the principal contractors only, while the ones that need protection most are the small subcontractors who may have to close up shop unless they can obtain a speedy settlement and an advance to tide them over. A problem may arise in some of the smaller localities where banks may be compelled to assume larger risks than are warranted. The Council does not have any final opinion as to how all these problems are to be met but would be very glad to know if the Board has reached any conclusions.

McKee points out that the war loans and advances were made under an Executive Order for the purpose of war production only. The services have no power to make advances in those cases where production has been completed or the contract is cancelled. VT loans are not entirely satisfactory, but out-and-out terminal loans will require legislation, and this is now being asked. Until such legislation is enacted, it will be impossible to have any advances made for the purposes of carrying over the period following cancellation.

Brown points out that the Government has been making advances to the International Harvester Company to settle with the subcontractors on the $400,000,000 Bethendorf Plant contract. The International Harvester Company is evidently being used as a test case. If a breakdown is to be avoided it will be necessary to provide some form of automatic advances without waiting for detailed audits and the like. Undoubtedly, there will be abuses but such a situation would not be as serious as one resulting from a general breakdown of our industrial machinery.

Draper thinks the armed services are building up a very good staff to handle the problem connected with the cancellation of contracts.

Brown. There is no danger as long as the war lasts, but comes general termination, then he rather suspects the forces to handle the problems will be inadequate.

Kurtz. A contractor who pledged receivables and the like can obtain a loan but there may be much money due the subcontractors. It has often been impossible to make physical inventories and in some cases estimates may be proved to have been very wrong. The prime contractor ought to be required to settle with the subcontractor without certification on a basis similar to the one that has enabled him to be accommodated. If this isn't done the prime contractor in some cases may try to hold up the subcontractors. It must be remembered that banks do not have staffs sufficiently adequate to arrange VT or V loans for every small contractor. The Board should insist that prime contractors be obliged to take care of subcontractors.

Draper says the Army is familiar with the problems involved.

Brown wants to know if the Board is completely in touch with the situation while the thinking of the armed forces is in the "jelling" stage. The process seems to be proceeding rapidly.

McKee says the Board has been trying to keep in touch with the situation for the last 6-8 months.

Brown points out the danger in the case of small people or corporations, say those with a capital up to $1,000,000, all of it perhaps in brick and mortar. Very few of these people have V loans and they don't want them, but they will take terminal loans.

McKee is of the opinion that the armed forces know that elasticity is required and that they plan to ask for needed powers very shortly.

Harrison says the whole group would be relieved to know how seriously the War Department is concerned about these problems and how much they are trying to coordinate with other departments.

McKee points out some other problems. The Government may own the machinery and plant; the owner may wish to buy the machinery but the Government can sell only on bids, so the machinery may be shipped to some place where it may have little value. There ought to be some arrangement by which the owners of a plant can buy machinery located in their own plant at a fair valuation without any bids being required.

Brown states the question of the Council has been answered and it is clear the Board is keeping in touch with developments.

REGULATION Q

Brown says the Board now has the "bear by the tail" but the Council would like to know what the Board is going to do with the tail. He is free to admit that the Council does not know what should be done.

Ransom says that in 1937 the Board thought it could take cases as they came up. The case in the Bulletin is that of a national bank and it is now the duty of the Comptroller of the Currency to take action. The next move is not up to the Board.

Wakefield thinks the mere publication of the opinion will have a salutary effect.

McKee says the opinion is now a guide for all bank examiners, and he believes the examiners will bring the situation to the attention of the board of directors of a bank and if the board of directors of the bank does not take action then the Comptroller of the Currency or some other agency will. He asks whether prior to the payment of interest the banks also absorbed exchange charges. He tries to show that absorption of charges now is an offset to the payment of interest, but the members of the Council were practically unanimous in stating this is not correct and that even when interest was paid on deposits there was general absorption of exchange charges.

INTERNATIONAL MONETARY STABILIZATION

Brown says all attending the Council meeting yesterday were opposed to all of the three plans: the Keynes Plan, the White Plan, and the Canadian Plan. The Treasury has asked for comments and so the Council has asked its Executive Committee to draw up a memorandum at an appropriate time and to submit such directly, or through the Board, to the Treasury. Everyone recognizes the need for stabilization and for getting rid of bilateral agreements. The Council, however, believes more can be attained by pound sterling-dollar stabilization in which would be included the Canadian dollar. Other countries would come in as their respective domestic situations became stabilized. He feels the White and the other plans would compel the interference by the Treasury and the Federal Reserve System in tariff policies, stabilization of cost of living, and the like. If our country came in there would be many defaults, and it would be much better for the United States to make rehabilitation loans or gifts, otherwise international bad will would be created. The serious situation at the moment is the British one and this should be taken care of first. Also, we can not do much until more is known about the Russian attitude.

China must ultimately come in. He pointed out the Council yesterday had been amazingly unanimous in its views. At the Chicago conference on August 26 of this year it was obvious that most of the audience were opposed to the plans presented.

Ransom agrees that this is not the time and place to argue out the whole problem, but he would be glad to hear more of the attitude of the Council.

Harrison feels the plans are untimely and premature and that the cart has been put before the horse. The first step is to stabilize domestic economies in the various countries. At a given date the exchanges are apparently to be fixed arbitrarily with the result that the whole plan may be gutted at the very outset. Procedure must be gradual.

Kurtz thinks the Keynes Plan is positively insulting to our intelligence. Apparently the fact is not taken into consideration that in a decade or so the Russian rouble together with the American dollar may be the leading currencies in the world.

Fleming believes discussion is helpful but doesn't think that any of the plans submitted can ever pass Congress. Also, we had better first of all bring about stabilization here at home. Apparently, under these plans, good and bad debts are all to be treated alike.

Evans points out the seriousness of the British situation resulting from the loss of foreign investments.

Harrison agrees very much that the first situation to be taken care of is that of Great Britain with its huge blocked accounts. In fact, the British situation offers more difficulties than others.

Huntington says discussions are desirable, but it is a pity the discussions should be based upon such impracticable plans as have been presented. He says there must be a sharp separation between long and short term loans, but the plans do not make this distinction very clear.

Gifford says the plans are likely to create international animosity.

Young and Wallace have no comments to make.

Brown asks the Board about the inquiry made by the SEC which he brought to the attention of the Council at its meeting yesterday. The Board had not heard of this action of the SEC and was evidently disturbed by it. It agreed to find out what it was all about.

The members of the Board stated it would be agreeable to the Board to have the Executive Committee of the Council meet with them on October 6.

The meeting adjourned at 1:15 P. M.

At 2:30 P. M. the Council reconvened in the Board Room of the Federal Reserve Building.

All members of the Council including the Secretary were present except Messrs. Spencer, Clark, and Adams.

Dr. Goldenweiser appeared before the meeting to discuss the present situation. We have now a national income of between $145 and $150,000,000,000 based on the current price level. Taxes have diminished the amount somewhat, but nevertheless the income is still tending to go up. Production is probably stabilized but prices will increase although there is nothing catastrophic about it. The industrial production behind all this amounts to about $203,000,000,000. Before the outbreak of the war in Europe, industrial production was about $100,000,000,000, and at the time we went into the war had gone up to about $130,000,000,000 - all of this on the 1935-39 base. The present index is no longer valid and a revision of the index which takes account of the development of industries which were not included when the previous index was prepared would show that industrial production now amounts to $240,000,000,000 or about two and one-half times what it was when the war began. It is obvious great progress has been made. It is likely we have reached the climax of output and no more is to be expected. Unfortunately, the increase of currency is not limited by physical factors, and the increase of this is likely to continue. Undoubtedly, a large part of the funds required by the Treasury will be obtained by borrowing from banks, so there is likely to be a constant growth of deposits and currency. There has been a 25 per cent increase since 1940 in the cost of living although a very small decrease in the last few months. However, there is likely to be a further increase, but it should be pointed out that the situation is not nearly as bad as it was in the corresponding period of the last war. The machine may not have worked very well, but it has worked. An enormous amount of money is still idle. It isn't being hoarded and isn't exactly being saved, but it isn't used although it must be confessed the lines of demarkation are not always clear. The reason so much money is not being used is that new automobiles and new house equipment are not available, and these are apt to be two of the principal items on which money is spent. He does not fear inflation as much as many do. The increase of taxes has been great enough to have given people a shock. Stocks in department stores are high, but the supply of new goods is diminishing so that stocks are likely to go down. Monetary trends are definitely inflationary, and he believes we should have forced savings and similar devices. After the war it will be important to keep up controlls for a time. More than the inflationary danger which we are fighting is the danger of unemployment after the war. The labor forces next year will consist of approximately 66,000,000 people of which 11,000,000 are in the armed forces. Perhaps about one million are unemployed which simply represents those incapable of working and a kind of a float; there are 12,000,000 in agriculture. After the war the armed forces may go down 5-6,000,000 people. There are now 11,000,000 people working in steel and munitions, and this number may go down 5,000,000. This will leave us with a problem of finding employment for anywhere between 15 and 18,000,000 people. Of these, perhaps 5-6,000,000 normally do not work, such as married women, although many of those who formerly did not work will wish to keep on working. So, the most important question we face is that of absorbing people and if we are not able to do that, we may have a deflation more dangerous than inflation. Hansen says cities should be rebuilt, but it is very unlikely this will be done on any large scale. A large mass of unemployment would be fatal to our political and economic system, and the situation will require great governmental wisdom. The deflationary movement may make itself felt possibly in six to nine months after the war. To a certain extent this situation will be helped by the fact that the war is likely to end in two stages. If we cannot in the long run prevent serious unemployment we are likely to have either communism or facism in this country. We may be able to do more work for foreign countries and we may give or lend them on long terms, but we should not do anything except what is to our own interest. We may find it even advantageous to give much away. In the '30s we sold goods for about $18,000,000,000 for which we received gold which we cannot use. In the long run, we ought to have more imports and less exports.

Before stabilization plans can work there must be agreement between Britain and the United States as to the rate of exchange between these two countries. Beyond that, all smaller countries must be told that their exchanges will be taken care of and they will be given small quotas, if these are used up they will be compelled to reform their internal economic systems. He believes it will help many countries to restore their own industries if they be given some margin to take care of their currency. He doubts whether this can be done on a country to country basis and therefore is opposed to the proposal made by John H. Williams.

Gifford asks whether deficit financing is to continue after the war. Goldenweiser believes we should work toward a balanced budget and a reduction of our debt. If we can have a national income of $150-160 billion the national debt will not be a problem. The problem is to keep up our own production, but if not, then we shall have to increase debt.

Kurtz. If the debt service amounts to $5,000,000,000, the Government takes back in taxes about 25 per cent leaving a net of $3,750,000,000 which is just about 10 per cent of the total tax intake this year

Goldenweiser doubts that E bonds will be redeemed on as large a scale as is sometimes supposed. To be sure, if everyone should rush to redeem his bonds immediately after the war it would create a serious situation. There has been some increase in the hoarding of currency. Circulation is now $18,800,000,000 which includes currency in banks. In recent months, the large denominations have shown striking increases and it looks as if about $100,000,000 a month is being hoarded.

The meeting adjourned at 3:45 P. M.