MINUTES OF MEETING OF THE EXECUTIVE COMMITTEE OF THE FEDERAL ADVISORY COUNCIL

June 26, 1946

At 11:00 A.M., the Executive Committee of the Federal Advisory Council convened in the Conference Room of the Federal Reserve Building, Washington, D. C., on Wednesday, June 26, 1946, the President, Mr. Brown, in the Chair.

Present: Mr. Edward E. Brown, President, Mr. Charles E. Spencer, Jr., Vice President; Messrs Howard A. Loeb (Alternate for Mr. David E. Williams), John H. McCoy, A. L. M. Wiggins, and Herbert V. Prochnow, Acting Secretary.

Absent: Mr. John C. Traphagen.

The Executive Committee discussed some sections of the Annual Report of the Board of Governors, particularly those relating to the amount of government bonds held by commercial banks.

The Executive Committee commented favorably regarding the active support which the Board of Governors had given to the policy of reducing government balances and using the funds for the retirement of the government debt.

There was a brief discussion regarding (1) the proposal of the Board of Governors for the reclassification of reserve cities, (2) the revised Bank Holding Company Bill and (3) the subject of loans to small business, particularly in relation to activity in this field on the part of government agencies.

The meeting adjourned at 12:00 noon.

HERBERT V. PROCHNOW
Acting Secretary.

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

June 26, 1946

At 12:20 P.M., a joint conference of the Executive Committee 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; Governors M. S. Szymczak, Ernest G. Draper, R. M. Evans, and James K. Vardaman, Jr.; Chester Morrill, Special Adviser to the Board of Governors; S. R. Carpenter, Secretary of the Board of Governors; George B. Vest, General Counsel; Woodlief Thomas, Director, Division of Research and Statistics; Leo H. Paulger, Director, Division of Examinations; Edward L. Smead, Director, Division of Bank Operations, and Robert F. Leonard, Director, Division of Personnel Administration.

Present: Members of the Federal Advisory Council:

Mr. Edward E. Brown, President, Mr. Charles E. Spencer, Jr., Vice President; Messrs. Howard A. Loeb (Alternate for Mr. David E. Williams), John H. McCoy, A. L. M. Wiggins, and Herbert V. Prochnow, Acting Secretary.

Absent: Mr. John C. Traphagen.

The President of the Federal Advisory Council expressed the appreciation of the Executive Committee to the Board of Governors for the active part the Board took in urging the use of Treasury balances for the reduction of the government debt. There was also a discussion regarding the possibility of staggered rates on loans, secured by governments, which Federal Reserve banks may make to member banks. The schedule of staggered rates would provide for lower rates to member banks which borrowed on short-term government obligations and higher rates when borrowings from the Federal Reserve banks were against longer-term government obligations. The Executive Committee believed the psychological effect would be that banks would tend to acquire more short-term securities for use in the event it became necessary to borrow from the Federal Reserve banks.

There was a discussion covering various aspects of the revised Bank Holding Company Bill and also of the various plans for extending loans to small businesses through government agencies.

The meeting adjourned at 1:35.

HERBERT V. PROCHNOW
Acting Secretary.

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

H. V. P.

The Acting Secretary's notes on the meeting of the Executive Committee of the Federal Advisory Council on June 26, 1946, at 11:00 A. M., in the Conference Room of the Federal Reserve Building. All members of the Executive Committee of the Federal Advisory Council were present except Mr. John C. Traphagen; Mr. Howard A. Loeb served as alternate for Mr. David E. Williams.

RATES ON LOANS TO MEMBER BANKS

BROWN. The Board of Governors in its recent Annual Report to Congress has suggested that it may be necessary to require commercial banks to hold more short-term Government securities and limit the amount of long-term Government bonds which commercial banks may hold. Brown believes it may be possible to obtain the objectives which the Board has in mind without the necessity of legislation. He suggests the setting up of a schedule of staggered rates on loans which are secured by Government securities and which member banks obtain from the Federal Reserve Banks. For example, loans secured by Government obligations having a maturity of one year or less might be made at a rate of one per cent; loans secured by governments having a maturity of one to two years might be made at 1-1/4 per cent; loans secured by governments having a maturity of two to three years might be made at a rate of 1-1/2 per cent. The rate on loans secured by Governments with a maturity of three to four years might be 1-3/4 per cent, and loans secured by governments with a maturity of four to five years might carry a two per cent rate. It might be possible to go even higher for still longer maturities. Brown believes the result of staggered rates of this kind on loans secured by governments would result in banks holding more short-term securities. In the event it became necessary to borrow they would be in a position to obtain a more advantageous rate.

LOEB asks whether a proposal of this kind would be satisfactory to Eccles in place of the program he has suggested. Loeb comments that Brown's idea would require no statutory action.

WIGGINS thinks it is an idea well worth discussing with the Board.

BROWN believes staggered rates of this kind would lead well-run banks to arrange their portfolios so they could borrow at the best rates in the event of necessity.

MCCOY thinks the idea has real merit and would accomplish what the Board has in mind without adopting the proposals which the Board has discussed in its annual report.

WIGGINS points out that there may be a demand for increasing regulation of the banking system and that this could go so far as to be very detrimental to banks.

MANAGEMENT OF THE PUBLIC DEBT

BROWN believes it would be desirable to express appreciation to the Board again for its active support of the policy of reducing Treasury balances and using the funds for the retirement of the government debt. He points out that it has had the effect of tightening somewhat the very cheap money rates. He mentions that rates to government bond dealers have recently been fixed at 7/8 per cent in Chicago and that loans to these dealers have now risen from 1/2 to 7/8 per cent. He also mentions that many banks have had to sell their holdings of 7/8 per cent certificates to meet the calls.

WIGGINS comments favorably on Snyder's speech yesterday when he became Secretary of the Treasury. Snyder urged the desirability of balancing the budget, and doing even better if possible. He placed himself clearly on record in this respect as Secretary of the Treasury.

CLASSIFICATION OF RESERVE CITIES

BROWN asks whether the Executive Committee should inquire regarding the classification of reserve cities. He believes that the matter is dead at present and that it might be advisable not to bring up the subject now.

MCCOY states that he talked with Ray Gidney, President of the Federal Reserve Bank of Cleveland, after the meeting of the Presidents of the Federal Reserve banks with the Board. Gidney informed him that the matter was considered dead.

WIGGINS comments that the Board's annual report mentions the possibility of having the same reserve requirements for all banks.

LOEB believes that this particular suggestion of the Board as well as other points in the annual report need more complete explanation.

BANK HOLDING COMPANY BILL

BROWN. In connection with this bill, Brown mentions that Eccles had stated at the last meeting of the Council and the Board that he would not give testimony before Congress on the bill now inasmuch as the bill would not be considered at this session of Congress.

WIGGINS thinks the present bill has a number of weaknesses.

BROWN states that Robertson of the Treasury is opposed to the whole concept of the bill. He understands Harl is also against the bill.

WIGGINS believes that there are at least two essential points which should be kept in mind in any bank holding company legislation: (1) the bill should be reasonably complete in what it specifies and requires and leave less to the discretion of the authorities who administer it; and (2) a holding company should probably not be permitted to acquire banks outside of the state in which the headquarters of the holding company are located.

BROWN comments that he is concerned about the possibility of a bank being called a holding company because estates in its trust department may have large bank stock holdings.

MCCOY believes this is important not only to large banks with trust departments, but also to many small banks.

LOEB states that if banks do not get back of some reasonable legislation the situation may develop to the point where it will lead to the nationalization of the banking system.

WIGGINS agrees.

SPENCER also agrees. He states that if banks do not help in working out some type of reasonable legislation it may be said in the event of severe depression or trouble that the bankers are to blame for having opposed all legislation.

WIGGINS thinks this bill may lead to nation-wide holding companies.

MCCOY reports that since the holding company bill was announced some groups have begun to purchase banks in Ohio.

LOANS TO SMALL BUSINESSES

BROWN reports that some time ago Wallace organized a Business Advisory Committee of the Department of Commerce. The Committee has recently prepared a report, which apparently has not yet been published but which favors in substance the extension of loans to small businesses, with a 90 per cent guarantee by the Federal Reserve System.

SPENCER states that this is apparently related to some discussion which he has heard about changes in Section 13 and 13b of the Federal Reserve Act.

WIGGINS thinks 13b should be repealed.

BROWN states that the theory of the Department of Commerce Committee presumably is that the smallest businesses should borrow on the same basis as large, well-established businesses. In this connection, Brown mentions that he has also discussed with some of the men who make the policy for the Reconstruction Finance Corporation the plan which the RFC has for loans to small businesses. Brown expressed to these men his disapproval of the general idea. He believes it is desirable for the Executive Committee of the Council to inquire of the Board regarding these proposals for loans to small businesses as well as the reports of a possible revision of Section 13 and 13b of the Federal Reserve Act.

The meeting adjourned at 12:00 noon.

On June 26, 1946 at 12:20 P. M., a joint meeting of the Executive Committee 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.

All members of the Executive Committee were present except Mr. John C. Traphagen; Mr. Howard A. Loeb served as alternate for Mr. David E. Williams. The following were present from the Board of Governors: Chairman Eccles, Governors Szymczak, Draper, Evans and Vardaman; also, Messrs. Morrill, Carpenter, Vest, Thomas, Paulger, Smead and Leonard.

MANAGEMENT OF THE GOVERNMENT DEBT AND RATES ON LOANS TO MEMBER BANKS

BROWN states that the Executive Committee of the Council wishes to express appreciation to the Board for the active part the Board took in urging the use of the Treasury balances for the reduction of the government debt. This program is progressing even more rapidly than had been anticipated. In connection with the annual report which the Board of Governors has made to Congress, it is noted that the Board has mentioned the possibility of requiring commercial banks to hold a certain amount of short-term government obligations and of restricting the amount of longer-term obligations which the commercial banks may hold. The Executive Committee would like to suggest a program of staggered rates on loans, secured by governments, which the Federal Reserve banks may make to member banks. It is suggested that loans secured by government obligations having a maturity of less than one year might carry a rate of one per cent; loans secured by government obligations having a maturity of one to two years might carry a 1-1/4 per cent rate; loans secured by government obligations having a maturity of two to three years might carry a rate of 1-1/2 per cent; loans secured by government obligations having a maturity of three to four years might carry a rate of 1-3/4 per cent, and those secured by government obligations having a maturity of four to five years might carry a two per cent rate. This program could be projected for longer maturities with still higher rates on the loans. A schedule of staggered rates of this general character would lead well-managed banks to hold more short-term paper for use in the event it became necessary to borrow. At least the psychological effect would be in the direction of acquiring more short-term securities for use in the event borrowing became necessary.

ECCLES asks whether this plan could be applied not only to government bonds but also to other longer-term bonds, for example, to agricultural paper. He thinks that some banks have made term loans and extended credit for relatively long periods on a basis which is not sound.

However, he believes Brown has in mind a staggered rate schedule which would apply on borrowing against government obligations--a penalty rate and not a preferential rate.

BROWN comments that if the banks knew they had to pay a higher rate on loans against longer-term government obligations, the banks would tend to hold more short-term paper. This is particularly true of the larger banks. Brown asks whether the economists of the Board have ever considered a program of this kind.

ECCLES asks Thomas whether a plan of this character has ever been discussed by the Board's economists.

THOMAS states that this particular proposal has not been discussed. Any discussion along these lines has been concerned simply with the effect of rate differentials. He states that rate differentials have not been as influential as had been anticipated in the past; banks generally carry enough of the preferred type of asset so that the rate differential is not especially effective.

ECCLES believes that the Board and its economists should certainly give consideration to this proposal. In connection with Brown's comments regarding the use of the Treasury balances for the retirement of the debt, Eccles is inclined to believe that the policy will not change and that Snyder, as the new Secretary of the Treasury, will continue to use the excess cash balances to retire government debt. He believes that the Treasury officials and staff all approve this policy of using the large Treasury balances to reduce the debt. The Treasury will have at least $11 to $12 billion in balances after July. Eccles thinks that perhaps $9 to $10 billion of these balances will be used for debt retirement during the remainder of this year. He estimates that the banks will have to sell $3 billion of government obligations during the balance of the year in order to meet their reserve requirements. He also believes the pressure on bank reserves will help to stabilize bond prices. In the event it becomes necessary to take any further action the reserve requirements in the central reserve cities can be raised. A substantial surplus in the budget will likewise be of assistance if it materializes. However, if there should be any further monetization of the debt in the next six, eight or ten months, it will be necessary to have legislation to deal with the situation.

BROWN suggests that the Board give further consideration to the idea of the Executive Committee of staggered rates on loans secured by government obligations. He again expresses appreciation to the Board for the emphasis it placed upon the use of Treasury balances for the reduction of the government debt.

ECCLES states that the Board not only favored strongly the reduction of the debt by the use of Treasury balances, but that it had to resist the pressure of the Treasury in order to eliminate the preferential rate.

BANK HOLDING COMPANY BILL

BROWN asks whether there has been any reaction to the Bank Holding Company bill.

ECCLES. There has been no reaction since the meeting in May of the Federal Advisory Council and the Board.

BROWN states that McCoy reports that since the bill was introduced some individuals are buying up banks in Ohio in anticipation of the organization of holding companies on a national basis.

MCCOY advises that this development has just begun in Ohio.

ECCLES comments that Ohio is apparently late in getting started as this development was going on over the country for some time before the bill was introduced. There is nothing now to stop the organization of holding companies on a national scale.

VARDAMAN states that four groups in St. Louis are buying banks. He asks whether the bill has actually lead new groups to buy banks.

MCCOY reports that the bill is leading to the purchase of banks in Ohio.

SZYMCZAK asks whether there is anything wrong with this development in Ohio.

BROWN states that it may involve the question of possible monopolistic tendencies.

WIGGINS thinks it would be desirable to prohibit holding companies from buying banks across state lines. He thinks holding companies should not be allowed to buy banks outside the state in which the head office of the holding company is located.

ECCLES believes this is the position also of the Comptroller of the Currency. (Szymczak left the meeting at 12:50 P. M.) Eccles states that it is one thing to freeze the situation, but if that is not desirable, the Board should have discretion in administering the provisions of the bill.

BROWN comments that the Executive Committee has agreed that something should be done in connection with certain aspects of the holding company situation.

ECCLES states that there are so many different ideas about what should be done that it is possible nothing will be done. If the Treasury, the American Bankers Association, the holding companies, the independent bankers, and others all have conflicting ideas, it is possible that nothing may be accomplished.

WIGGINS states that he is surprised not at the disagreement, but at the widespread agreement regarding many phases of the matter.

ECCLES states the Board has no objection to a freeze.

VARDAMAN points out that one St. Louis group may expand so they will operate from New Orleans to Chicago.

ECCLES does not favor a limitation to state lines. He does not believe that the state lines necessarily comprise economic units. Federal Reserve districts or Federal Reserve branch areas would make a better grouping.

VARDAMAN would prefer legislation by Congress on this matter. He wishes Congress to give instructions to the Board. He asks, for example, just how a group like the St. Louis group, which is conservatively managed, could be restricted by the Board, if the discretion for administering the act is left largely in the hands of the Board.

ECCLES believes that limiting the operation of holding companies to Federal Reserve districts or Federal Reserve branch areas is better and more logical than a limitation along state lines. Originally he preferred a freeze, but there is no possibility of getting it.

BROWN. If the Board wishes to do something along these lines, he believes there would be more agreement if the following principles were followed in general: (1) a freeze on existing holding companies and branches; (2) discretion within the Board to limit expansion to Federal Reserve branch areas.

LOEB asks whether any states prohibit bank holding companies.

ECCLES. No. There is nothing to stop a company from buying bank stocks and there is no objection to this procedure from an investment standpoint. However, it is definitely objectionable when it is done for the purpose of managing banks and when there is no control over the holding company operations. He does not believe the same holding company can manage banks effectively, for example, in Texas, Massachusetts and Illinois when the operations are under such widely varying economic conditions and when the management is far removed from the banks it operates.

LOANS TO SMALL BUSINESSES

BROWN asks whether any consideration has been given to the revision and consolidation of Sections 13 and 13b of the Federal Reserve Act. He also asks whether the Board is familiar with a report of the Business Advisory Committee of the Department of Commerce dealing with loans to small businesses.

DRAPER reports that he has been a member of the Business Advisory Committee and four or five days ago saw a copy of the report. He believes that close to 40 per cent of the proposals in the report are not sound, but he does not believe there is any possibility of their being seriously considered in the near future.

ECCLES reports that the Board has been giving some consideration to changes in Sections 13 and 13b. He reports that there is a conflict between the small and large banks. The small banks wish to make loans in excess of their legal limits, and they wish the Federal Reserve banks to take part of the loans. If the Federal Reserve banks do not arrange to take care of such situations, the Reconstruction Finance Corporation blanket idea may really develop in a large way.

LOEB asks whether the Board does not have the power now to take care of these situations.

ECCLES replies that the Board does not have adequate power. He believes that Section 13b should be repealed. He reports that the small banks like the Reconstruction Finance Corporation blanket idea. If the law were changed, the small banks could take care of their larger customers.

BROWN states that the Department of Commerce apparently believes that little businesses should borrow on the same basis as big businesses.

DRAPER believes that the Department of Commerce proposal for loans to small businesses looks pallid compared to the RFC plan.

WIGGINS states that the RFC idea is not in the best interests of the banking system.

The meeting adjourned at 1:35 P. M.