

FEDERAL RESERVE BANK
OF NEW YORK

[Circular No. 2680]
September 1, 1943

THIRD WAR LOAN

BANK INVESTMENT OF TEMPORARILY IDLE FUNDS
LOANS ON GOVERNMENT SECURITIES

*To all Incorporated Banks and Trust Companies
in the Second Federal Reserve District:*

During the Third War Loan drive in September, a substantial amount of the private deposits of commercial banks will be transferred to war loan deposit accounts in payment for Government securities subscribed for by customers. Since there are no reserve requirements with respect to war loan deposit accounts, this transfer will normally result in a decline in the required reserves of the banks having such accounts and an increase in their excess reserves. The increase in excess reserves, however, will be only temporary. Government funds in war loan deposit accounts will be withdrawn by the Treasury in instalments as needed and, although they will be almost immediately returned to the banking system in the form of private deposits through Government disbursements, not all banks will get back the full amount of the funds withdrawn. Furthermore, since reserves are required against private deposits, bank reserve requirements will rise, as this transfer from war loan deposits to private deposits takes place, and excess reserves will diminish.

In these circumstances, banks are urged to invest their temporarily idle funds in Treasury bills, which are ordinarily the best medium for adjusting for changes of this nature. Banks that have sold bills to the Federal Reserve Banks under option to repurchase can invest their funds by repurchasing these bills. Other purchases of bills can be made by bidding for new issues and by purchasing bills in the market. As excess reserves subsequently decline, banks can sell bills to the Federal Reserve Banks under option.

In following this policy, banks will not impair their ability to subscribe for the new Treasury securities which will be offered for exclusive subscription by commercial banks for their own account shortly after the close of the Third War Loan drive. Subscriptions to these issues will not affect the level of reserve requirements and need not affect excess reserves at that time. Banks having war loan deposit accounts can pay for all of their purchases of these securities by credits to such accounts.

The Third War Loan will be a drive to sell Government securities to investors—investors other than commercial banks. It is desirable to eliminate, as far as possible, speculative purchases of securities offered during the drive. Bank loans for speculative purchases of Government securities are not an appropriate part of the Third War Loan drive. Bank loans to investors to help finance the purchase of Government securities, if such loans are made in accord with the joint statement issued by the National and State bank supervisory authorities in November 1942, are an appropriate part of the drive. That statement reads in part as follows:

“In connection with Government financing, individual subscribers relying upon anticipated income may wish to augment their subscriptions by temporary borrowings from banks. Such loans will not be subject to criticism but should be on a short term or amortization basis fully repayable within periods not exceeding six months.”

Loans made on any other basis to facilitate the purchase of Government securities during the drive, particularly where there are indications that such purchases may be speculative in character, should be at rates high enough and with a margin of collateral substantial enough to discourage speculators.

ALLAN SPROUL,
President.