NEW PLAN FOR STATING THE RESERVE POSITION OF FEDERAL RESERVE BANKS.

Section 16 of the Federal Reserve Act contains the following provision on the subject of the reserves required to be maintained by Federal reserve banks:

"Every Federal reserve bank shall maintain reserves in gold or lawful money of not less than thirty-five per centum against its deposits and reserves in gold of not less than forty per centum against its Federal reserve notes in actual circulation."

and

"That when the Federal reserve agent holds gold or gold certificates as collateral for Federal reserve notes issued to the bank such gold or gold certificates shall be counted as part of the gold reserve which such bank is required to maintain against its Federal reserve notes in actual circulation."

It seems clear from this that the law contemplates that there shall be maintained a separate reserve of not less than 35% against deposits, and a separate reserve of not less than 40% against Federal reserve notes in actual circulation, in each Federal reserve bank.

Section 11 of the Federal Reserve Act provides:

"The said board shall publish once each week a statement showing the condition of each Federal reserve bank and a consolidated statement for all Federal reserve banks. Such statements shall show in detail the assets and liabilities of the Federal reserve banks, single and combined, and shall furnish full information regarding the character of the money held as reserve and the amount, nature and maturities of the paper and other investments owned or held by Federal reserve banks."

It would seem that the provision of the Act requiring that the condition statement of the Federal reserve banks "furnish full information with regard to the character of the money held as reserve", read in conjunction with the preceding provision regarding reserves quoted from

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Section 16, should be construed as requiring that the Federal Reserve Board should publish in its weekly statement the state of the reserves held respectively and separately against deposit liabilities and Federal reserve notes.

This the Board is not doing. It has been the practice since January, 1918, (when the present practice was adopted as a war-time expedient) to state the reserve position of the Federal reserve banks by computing the ratio of their holdings of reserve moneys against their deposit liabilities and note issues combined, although there appears to be no warrant in the Act for this method, unless it be purely for purposes of theoretical comparison.

The Federal Reserve Board has plenary power, under the terms of Section 16 of the Federal Reserve Act, with respect to the issue of Federal reserve notes and the character of the security against which notes will be issued by it to reserve banks:

"The board shall have the right, acting through the Federal reserve agent, to grant in whole or in part, or to reject entirely the application of any Federal reserve bank for Federal reserve notes."

"The said Federal Reserve Board may at any time call upon a Federal reserve bank for additional security to protect the Federal reserve notes issued to it."

It appears to be clearly within the discretion of the Federal Reserve Board, therefore, to determine from time to time against what security it will authorize the issue of Federal reserve notes, and thus, in its discretion, when conditions seem to the Board to require it, to issue such notes only against gold collateral.

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In other words, it is within the power of the Federal Reserve Board to determine the amount of the gold reserve that shall be carried against Federal reserve notes.

The extraordinary accumulation of gold by the Federal reserve system during the past two years and more, amounting to approximately 1200 millions, to my mind makes more urgent than ever the inauguration of a procedure which is not only in conformity with the requirements of the law, but in harmony with a good and effective regulation of the currency and a good administration of credit by the Federal reserve system. The initiative should be taken by the Federal Reserve Board.

I propose, therefore, that beginning say April 1 or such other date as the Board may determine upon, the weekly statements of the Federal reserve banks, both the separate and the consolidated, show the reserves actually carried against deposits and the reserves actually carried against notes.

(Note: If it is thought desirable, purely for purposes of theoretical comparison, the weekly statement might carry in a footnote the ratio of the reserve moneys of the Federal reserve banks against combined note and deposit liabilities.)

An examination of the records of the Board shows that the actual allocation of reserve moneys as of March 7, 1923, between the banking department of the Federal reserve banks and the Federal reserve agent's department, or, otherwise stated, between the deposit reserve and the note

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reserve, was as follows:

TABLE I

	Reserve ratio against deposits	Reserve ratio against notes
Boston	53.6%	88.6%
New York	60.4	111.5
Philadelphia	54.5	84.8
Cleveland	61.3	90.0
Richmond	70.8	77.3
Atlanta	48.5	89.4
Chicago	49.8	94.0
St. Louis	40.0	95.5
Minneapolis	67.2	84.4
Kansas City	46.1	86.6
Dallas	49.2	49.7
San Francisco	44.8	88.0
System	55.3	94.3

This statement shows the actual allocation of reserve moneys, It is, however, never published, and is not known even to many persons within the Federal reserve system.

This statement, it is highly interesting to note, shows that the reserve banks, under the necessities of the extraordinary situation occasioned by the heavy influx of gold during the past two years and the liquidation of loans and discounts at Federal reserve banks, have pretty generally tendered gold to Federal reserve agents as the principal security for Federal reserve notes issued to the banks.

In publishing a weekly statement showing the deposit reserve and the note reserve separately, we might start with the actual existing allocation of reserve moneys, or we might consider some slight departure from the existing allocation more in accordance with what the Board might believe to be an ideal apportionment. I offer therefore the following plan for the

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consideration of the Board:

TABLE II

Table based on the weekly statement for March 7, 1923, showing the deposit and note reserve ratios for each of the banks and for the twelve banks combined if the reserve moneys were so allocated between the deposit reserve and the note reserve as to make the minimum deposit reserve ratio shown for any reserve bank 50%.

(In millions)	Deposit reserves	Deposit reserve ratio	Note reserves	Note reserve ratio
Boston	63	50.0	184	90.6
New York	491	69.5	570	100.0
Philadelphia	59	50.0	175	87.1
Cleveland	79.5	50.0	227.5	93.1
Richmond	32	50.0	80	92.0
Atlanta	29.5	50.0	109.5	88.3
Chicago	143	50.0	371	94.0
St. Louis	39	50.0	75	86.2
Minneapolis	29	51.8	56	100.0
Kansas City	43	50.0	53	81.6
Dallas	28.5	50.0	15.5	50.0
San Francisco	74.5	50.0	173.5	84.6
System	1111.0	57.2	2090.0	92.7

Under the above allocation, no bank would have a reserve of less than 50.0%, which is the lowest reserve shown under the Board's present form of statement for any of the banks, namely, in the case of the Federal Reserve Bank of Dallas. The highest deposit reserve ratio would be shown by New York, to-wit, 69.5%, and two banks, to-wit, New York and Minneapolis, would show 100% note reserves.

In the event that it should be felt that this form of statement showed too great a disparity between the deposit reserve ratio of the New York bank and the other banks, the deposit reserve of the New York bank could be brought down by New York's purchasing open market investments from other

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reserve banks to an amount sufficient to bring down the New York deposit reserve ratio to the average for the system, to-wit, 57.2%. The way in which this operation would work out is shown in the following table:

TABLE III

Calculation of adjustment of open market holdings of Federal reserve banks through transfer of sufficient holdings to New York to bring the New York deposit reserve ratio down to the system average (57.2%). Based on the weekly statement for March 7, 1923.

(In millions)	Actual holdings of open market purchases	Change in holdings to bring down N.Y. ratio to 57.2%	Adjusted holdings after change	Deposit reserves before adjustment	Deposit reserves after adjustment	Deposit reserve ratio before adjustment	Deposit reserve ratio after adjustment
Boston	40	-8	32	63	71	50.0%	56.3%
New York	55	+88	143	491	403	69.6	57.2
Philadelphia	58	- 8	50	59	67	50.0	56.8
Cleveland	76	- 8	68	80	88	50.0	55.5
Richmond	2	0	2	32	32	50.0	50.0
Atlanta	25	-3	22	29	32	50.0	54.2
Chicago	103	-20	83	143	163	50.0	56.9
St. Louis	39	- 8	31	39	47	50.0	60.3
Minneapolis	17	- 3	14	29	32	51.8	57.1
Kansas City	47	- 8	39	43	51	50.0	59.0
Dallas	34	- 3	31	28	31	50.0	54.8
San Francisco	67	-19	48	74	93	50.0	62.5
System	563	---	563	1110	1110	57.2	57.2

It is to be noted that in such a redistribution of the earning assets of the twelve banks, each bank would retain a sufficient volume of earning assets to make its expenses and dividends.

The allocation of reserve moneys thus proposed would show an average for the System of 57.2% for the deposit reserve ratio, and 92.7% for the note reserve ratio.

The greatest variations from the average for the system for the de-

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posit reserve ratio would be shown in the case of San Francisco (62.5%) and Richmond (50.0%).

For the note reserve ratio, the greatest variation from the average for the system, as shown in Table II, p. 5, would be in the case of Dallas (50.0%), New York (100.0%), and Minneapolis (100.0%).

Under the allocation of reserve moneys outlined above, and with a deposit ratio for the twelve banks combined of 57.2%, the twelve Federal reserve banks would be able to expand their loans to an amount of approximately 850 millions before the deposit reserve fell to 40%. Otherwise stated, for each drop of 1% in the deposit reserve ratio, the twelve banks combined would have an added lending power of approximately $50,000,000.

A. C. M. March 22, 1923.

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