TENTATIVE DRAFT - SUBJECT TO CHANGE

CONFIDENTIAL

MINUTES OF THE MEETING OF THE FEDERAL OPEN MARKET COMMITTEE HELD AT WASHINGTON, D. C., TUESDAY, OCTOBER 10, 1933.

The meeting was called to order at 3 p. m., there being present:

From the Federal Reserve Board
Governor Black, and Messrs. Hamlin, Miller, James, Thomas and Szymczak.

From the Federal reserve banks
Governors Harrison, Fancher, Martin, Geery, Hamilton, McKinney, Young, Norris and Calkins, Acting Governor Johns, and Deputy Governors Peple and McKay.

From the Federal Reserve Board Staff
Messrs. Morrill and Martin.

Governor Harrison outlined to the conference briefly the discussion which took place at the meeting of the executive committee in New York on September 21, at which time, he pointed out, the committee agreed that there was then little, if any, necessity for the further purchase of government securities from the point of view of the present credit and banking position alone. He referred to the fact that money rates in the principal centers are the lowest of any time in their history; that the borrowings of member banks are lower than at any time since 1917; that excess reserves are now at their highest level, about 800,000,000; and that in these circumstances it might well be argued that further purchases of government securities are no longer required as a means of pressure towards expansion of credit. The question for the conference to decide, therefore, was whether under these conditions there were other reasons, apart from the ordinary central bank objectives, for continuing open market purchases, and if so, in what amounts or at what rate.

Governor Black expressed the view that open market operations to date had no doubt been effective, as Governor Harrison had stated, in making for great ease in the credit position, and that they had also been a most important factor to date in minimizing the pressure for more drastic inflation; that all things considered, he thought it would be advisable to continue open market operations lest a cessation now might sooner or later force ~~the issue of greenbacks.~~ radical steps.

Mr. Miller questioned whether there was any real risk in further purchases of government securities, and expressed the opinion that we should continue them for a while at least. The only real question in his mind was at what rate they should be made, that is, whether at the same or a lower rate.

Mr. James felt that there was little that could be done that would be of effect until the various functions of the government were co-ordinated in repairing the banking position, and that we must also find ways of affording a compensatory return for money. In this connection, Governor Young expressed the view that it is possible to get money rates so low as to be a deterrent to its use. But apart from that, Governor Young said that in the present state of affairs, and possibly for political reasons, it might be advisable for a time to continue to buy securities but at as low a rate as is possible without precipitating other difficulties.

Governor Hamilton stated that most commercial banks are suffering from a loss of earnings. He felt that the program for the issue of capital stock to the Reconstruction Finance Corporation was an excellent idea, but it was difficult for him to see how the banks could use the money thus obtained.

Governor Young reiterated his belief that having commenced the program of open market purchases it might be harmful to stop entirely just now, but that we should ease off in our purchases, if possible, beginning this week. Governor Harrison questioned whether this particular week was a good week to begin reductions if only because of the possibly bad repercussion on the new Treasury issue to be announced on Thursday.

Governor Martin stated that while he felt that we should continue the program for the time being, nevertheless we must keep more and more in mind the necessity for giving banks an opportunity to make some earnings.

Governor Norris remarked that we have well over two billion dollars of government securities, which form over 95% of the assets of the Federal reserve banks. He also mentioned the fact that money rates are now so low that many banks have no incentive to make loans since many loans at present rates involve a risk with but little return. Furthermore he is of the opinion that the majority of the American public is against inflation and for sound money. In this connection he felt that the opinions expressed by the American Federation of Labor and the American Legion are significant, and that it is possible that the talk of inflation is more noisy than real. On the whole, however, he felt that we should be prepared to buy government securities for a few weeks or months longer, if necessary, pending the formation of a monetary policy, although if continued too long the only effect of them will be to weaken the banking structure of the country by reducing rates to a point which will yield little return to the banks and deter them from making loans. He called attention to the fact that increased employment depends in large part now on a revival of the heavy goods industries which in turn depend upon reopening of the capital markets.

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Mr. McKay stated that the Federal Reserve Bank of Chicago has participated in the program thus far reluctantly, and that the directors seeing no great good resulting from the program, felt that there was no need now to continue. He said, therefore, that his directors preferred not to proceed any further unless directly requested to do so under the terms of the Thomas amendment.

Governor Fancher said there was some question in his mind as to the advisability of changing the System policy at the moment although he favored doing so as soon as possible.

Mr. Hamlin concurred with the views of Governor Black and Mr. Szymczak who felt that we should continue the program at least until January 1. Mr. Thomas favored a continuation of the policy inasmuch as he feared that stopping purchases would be construed as a signal for deflation. Psychology, he said, is the largest part of the problem. He would, therefore, prefer to see purchases increased rather than reduced.

At 5 p. m. the Federal Reserve Board withdrew from the meeting and the Federal Open Market Committee continued its discussion.

Governor Harrison presented to the conference the preliminary memorandum as well as the Secretary's report of open market operations since the last meeting. Both were considered and ordered placed on file.

After further discussion of the arguments in favor of and against further purchases of government securities it was voted unanimously that the minutes of the meeting of the executive committee held in New York on September 21 be approved and ratified.

It was then unanimously voted that subject to the approval of the Federal Reserve Board, the authority granted to the executive committee at the meeting of the Open Market Policy Conference on April 22, (as amended,) to purchase up to $1,000,000,000 of government securities be continued and reaffirmed for the unused portion of the authority.

During the discussion of this resolution it appeared to be the opinion of all those present that from the point of view of the present credit and banking position alone, there was little, if any, necessity for further purchases of government securities, and that, therefore, it would seem to be advisable in the present circumstances gradually to reduce the rate of purchases as soon as and to the extent that it is possible to do so without adverse effect upon the government's program of recovery. It was recognized, however, that in view of existing uncertainties and the possibility of the development of new conditions or policies that cannot now be foreseen, the executive committee should be free, pending another meeting of the Federal Open Market Committee, to use its discretion as circumstances dictate.

At this point the executive committee took up for consideration the question of the amount of purchases for the current statement week, and it was voted that $35,000,000 should be bought. Mr. McKay voted in the negative and stated that in view of the action taken by his directors it would be impossible for the Chicago bank to participate in these purchases; whereupon all the other Governors present said that they would recommend that their banks take their pro rata share of the purchases which otherwise would have been allocated to the Chicago bank.

The meeting adjourned at 6:30 p. m.

The meeting of the Federal Open Market Committee reconvened Thursday, October 12, 1933, at 11:15 a. m.

Governor Harrison stated that in view of the discussion which had taken place in the past two days about the effectiveness of further open market operations under present conditions, he thought it would be helpful if the conference would formally express its views to the Federal Reserve Board regarding the usual objectives of open market operations, reviewing what had been accomplished thus far toward improving the banking position of the country and in creating a credit position which would make possible an expansion of both short time and long time credit as soon as there might be need or demand for it, and pointing out the deterrents to the desired expansion of credit in present circumstances. After further considerable discussion, the following resolution was unanimously adopted as an expression of the views of the committee:

"In their participation in the extensive open market program which the Reserve System has conducted for a number of months past, the Federal reserve banks have been actuated by their desire to contribute to the fullest extent within their power to the national recovery effort. In furtherance of that desire, and as a result of our observation of the open market

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figures for 2 wks later than in original memo.

operation, we believe that we may render a helpful service by recording our present views.

"The System's holdings of government securities now amount to the unprecedented sum of $2,344,000,000 (274), more than ten per cent of the Federal debt. Excess reserves of member banks are now nearly $800,000,000, member bank indebtedness to the Reserve banks has been reduced to the smallest figure since August, 1917, and short-time money rates have been forced down to the lowest level in our history. When to these facts it is added that the volume of currency outstanding is approximately $5,600,000,000 (5,595,000,000), far in excess of that outstanding in 1929, and that bank reserves are greater than at any previous time in our history, it would seem that our monetary problem today is not so much one of correcting a deficiency in the supply of basic money, whether by Federal Reserve credit or by government currency, as of achieving an effective use and turnover of the already existing supply.

"Open market operations, as a means of stimulating business recovery, are ordinarily designed to force banking funds, first, into the short-time money market, and subsequently, as short-time rates are lowered, into the intermediate and long-time capital markets. In the present instance, it seems clear that neither of these major purposes is yet accomplished.

"As to short-term credit, there are still grave obstacles both for borrowers and for lenders. Many business concerns, whose worth has been diminished by the unprecedented shrinkage in values and by several years of unprofitable operation have been either unable or afraid to draw upon the available credit supply. At the same time many of the banks, partly by reason of their former unfortunate experiences and partly by reason of new uncertainties incident to the inauguration of the deposit insurance and other features of the Banking Act of 1933, have felt it necessary to pursue a policy of extreme liquidity. The result is that, notwithstanding the Reserve System's open market purchases and the consequent large increase in bank reserves, loans and investments of member banks have been virtually stationary for four months, and net demand deposits are less today than at the end of May. In addition, some $4,000,000,000 of deposits remain locked up in closed or unlicensed banks.

"Not only has there been no expansion in the volume of short-term bank credit, but the desired pressure of funds into longer uses in the capital goods industries seems to be blocked by lack of confidence in the future position of the dollar and uncertainty with respect to monetary policy in general, and also by the liabilities imposed by the Securities Act of 1933 and the Banking Act of 1933. The capital issues market remains completely stagnant; and coupled with this (fact) is the further fact that the recovery in business from March to August, though unprecedented for extent in so short a period, revealed a serious lack of balance in the pronounced lagging of the capital goods industries, which are responsible for over 60 per cent of present unemployment. It is worthy of special mention, also, that during the recent recurrence of inflationary agitation the bond market lost one-third of its advance since March. The bearing of a declining bond market upon the condition of banks and upon the prospect for reviving the capital goods industries through the long-time money market requires no elaboration.

"In our judgment, these conditions indicate that the effectiveness of open market operations, in so far as banking and credit factors are concerned, will depend in large measure upon the early adoption of a broader program, designed to strengthen confidence and to encourage the flow of credit, both short-time and long-time, into uses which make for a well-balanced and enduring recovery."

The meeting adjourned at 1:15 p. m.

George L. Harrison,
Chairman.