A meeting of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System in Washington on Thursday, April 21, 1938, at 10:25 a.m.

PRESENT: Mr. Eccles, Chairman
Mr. Harrison, Vice Chairman
Mr. Szymczak
Mr. McKee
Mr. Ransom
Mr. Davis
Mr. Draper
Mr. Sinclair
Mr. Newton
Mr. Schaller
Mr. Peyton

Mr. Morrill, Secretary
Mr. Wyatt, General Counsel
Mr. Goldenweiser, Economist
Mr. Dreibelbis, Assistant General Counsel
Mr. Burgess, Manager, System Open Market Account

For the purpose of the Committee's records, Chairman Eccles referred to the recent developments in connection with the Government's program for the encouragement of business recovery, including the President's message of April 14 to the Congress of the United States, the President's radio address which was broadcast from the White House on the evening of April 14, the action of the Board of Governors on April 15 in reducing reserve requirements on all classes of deposits for all member banks effective at the opening of business on April 16 and the announcement thereof, released to the press for morning newspapers of April 16, which referred to this action as a part of the Government's program for the encouragement of business recovery, and to the announcement made by the Treasury Department on April 18 for release in the morning papers of April 19, that the inactive gold account had been discontinued. In the President's message to the Congress on April 14 the following statement was made:

> "The Administration proposes immediately to make additional bank resources available for the credit needs of the country. This can be done without legislation. It will be done through the desterilization of approximately one billion four hundred million dollars of Treasury gold, accompanied by action on the part of the Federal Reserve Board to reduce reserve requirements by about three-quarters of a billion dollars. The Federal Reserve Board informs me that they are willing to do so. These measures will make more abundant the supply of funds for commerce, industry and agriculture. By themselves, however, monetary measures are insufficient to start us on a sustained upward movement."

The Chairman stated that he had discussed with the Secretary of the Treasury this morning the considerations involved in such decision as the Treasury might make with respect to the utilization of the gold released from the inactive gold account; that he had an appointment to discuss the matter further with the Secretary of the Treasury at 12:30 today; and that the Secretary of the Treasury had in view a press conference at 5:00 o'clock at which he expected to make a statement as to what the program of the Treasury would be with respect to replacing or paying off maturing Treasury bills.

The Chairman then stated that he felt that the question of the policy to be pursued hereafter by the Federal Open Market Committee in the light of the changed situation had become one of very great importance; that the greatly increased volume of excess reserves had an important bearing upon the market for Government securities, and that in spite of the fact that there had been sold from the system account with a view to preventing a disorderly market more than $100,000,000 of bonds with corresponding purchases of bills and notes, the market had advanced very rapidly during the past few days and the short-term market particularly had gone up until the yield was negligible on notes and some bills were selling on a no-yield basis. He referred to the fact that the Treasury had announced the complete desterilization of gold in an amount aggregating approximately $1,392,000,000, together with the discontinuance of further sterilization, and that the resulting Treasury deposits had increased the Treasury balances at the Federal reserve banks and depository banks to approximately $2,300,000,000. He observed that the desterilization action had not yet created excess reserves and would not do so until the Treasury began making disbursements from its balances with the Federal reserve banks; that there were falling due each week $100,000,000 of Treasury bills until June 22, after which there would be $150,000,000 falling due each week until July 20 and that, in addition, there would be $250,000,000 of tax bills falling due in the middle of June and $620,000,000 of notes maturing on the 15th of June.

He stated that it was understood that the Treasury proposed to retire $50,000,000 of the maturing bills each week until further notice as well as the $250,000,000 of tax bills maturing in the middle of June. The result of this, he said, would be to increase excess reserves of member banks until the middle of June at the rate of $50,000,000 a week faster than would result from current net expenditures of the Treasury. He summed up the situation by saying that it appeared that with the retirement in June of the tax bills, about $600,000,000 would be added to excess reserves, sooner than would be the case if the Treasury were to wait until net expenditures produced that result, and that approximately $1,000,000,000 of the total of $1,400,000,000 of desterilized gold would be in excess reserves of member banks by the middle of June. He added that there very likely would also be additions to excess reserves by reason of further gold imports.

He pointed out that the proposed weekly retirement of bills would reduce the amount of such paper available in the market and at the same time increase the ability and desire of banks to make additional investments, with the result that, in the absence of opportunities to invest funds elsewhere, the banks would bid up the prices of the Government securities remaining on the market. He added that the Reserve system would have $39,500,000 of bills falling due on April 27; $36,500,000 on May 4; $54,500,000 on May 11, $59,000,000 on May 18, $55,500,000 on May 25, $48,500,000 on June 1, $34,500,000 on June 8, $19,000,000 on June 15, $31,000,000 on June 16, and $45,000,000 on June 17, and that the difficulty in replacing these bills would not be nearly as great if the Treasury were to refund in the market the full amount of its outstanding maturities as would be the case under the contemplated plan of retiring $50,000,000 each week.

On the other hand, the Chairman stated, if the system were to allow the bills in its portfolio to run off without replacement, the effect on excess reserves would be practically to offset the reduction in reserve requirements which had been made by the Board of Governors, and he felt that such action would be regarded as in effect nullifying the action of the Board in reducing reserve requirements or as nullifying to an equivalent extent the action of the Treasury in paying off maturing bills as a means of giving effect to the gold desterilization policy, with its consequent increase in the lending power of banks. The Chairman recognized the fact that the replacement by the system open market account of the maturing bills held by it would have a tendency to upset the market further but expressed the opinion that the Reserve system should not be held at fault for such a consequence; that the Treasury should be fully advised that the system could not accept responsibility for the condition in the Government bond market created by the Treasury's determination to pay off maturing bills; and that the system could accept responsibility for market conditions only if it had the full cooperation of the Treasury. He pointed out that while the proposed action of the Treasury involved a temporary reduction in the outstanding public debt, the Treasury would be under the necessity later on of increasing the debt at a much greater rate by reason of increased expenditures than would be the case if it replaced the maturing bills currently; that no one could foresee what the condition of the market would be when new borrowing became necessary; and that, in these circumstances, he saw no reason why the committee should assume responsibility for attempting to prevent the anticipated disorderly condition in the Government security market due to rapidly rising prices. He expressed the further view that, if banks continue to buy bonds in these circumstances, the system should not be held responsible for not interfering in the market; that the trend in the market was in the direction of much lower yields for Government bonds; and that, even if the system were to sell its entire portfolio of Government bonds, such action might not be sufficient to control the expected rise, and therefore might strip the system of practically all its earning assets without achieving the desired result.

There ensued a discussion of the policy to be adopted by the Committee to meet the situation. The opinion was expressed and concurred in by some of the members of the Committee that the system could not be expected to maintain its existing portfolio beyond the extent that replacement securities could be purchased on a no-yield basis or better. There was also consideration of the question whether the System would be justified in replacing maturing securities if such action would reduce bills as well as notes with maturities up to two years or more to a no-yield basis, and particularly since such replacements would tend to distort the relationship between short- and long-term rates, which relationship is as important an element in an orderly market as the general level of rates. It was pointed out that notes were being quoted at the present time on a no-yield or minus-yield basis for maturities up to a year and a half and that it was extremely difficult to get sufficient blocks of notes for replacement purchases.

With respect to the Board's action in increasing reserve requirements, the statement was made that while, following that action, there remained a large volume of excess reserves accompanied by extremely low rates of interest and an abundance of available funds, many people were under the impression that the Board's action was unduly deflationary, that therefore the System was in a position, in the opinion of a portion of the public at least, of resisting the recovery program, that for that reason the Board of Governors could not be motivated exclusively by the economic factors in the situation and disregard the psychological factors, and that the subsequent reduction of reserve requirements was believed to be in the best interests of the Federal Reserve System. Some of the members of the Committee referred to the fact that the Board of Governors and the Committee were differently constituted bodies, with separate statutory responsibilities, and stated that they felt that, therefore, the Committee was under the necessity of determining what course it should follow regardless of how the situation with which it was confronted was created.

Some of the members of the Committee stated that, while it apparently was the desire of the Administration to have the entire addition to excess reserves resulting from the termination of the inactive gold account made effective as promptly as possible, they felt that the Treasury should operate on a week-to-week basis and determine, in the light of developments, whether the policy of retiring bills should be continued.

There was also discussion of the questions whether, if no action be taken by the system to influence the market during the period of an advance, such action should be taken during a period of market decline, and whether, in view of the fact that up to the present time the policy of the system had been to endeavor to maintain orderly conditions in the Government securities markets, a reduction of from $200,000,000 to $400,000,000 in the System portfolio for the purpose of effectively continuing that policy could reasonably be interpreted as an effort to nullify the reduction in reserve requirements. In this connection, some of the members of the Committee took the position that the Committee should not abdicate its responsibility for maintaining orderly conditions in the Government securities market and that they did not believe that the Treasury or the Administration would wish the Committee to do so if they were fully informed as to the nature of the problem; that therefore the Secretary of the Treasury should be put on notice of the difficulties from the Committee's standpoint of the position with which it was confronted; and that the Treasury should be requested to modify its program with respect to maturing bills, thereby giving the Committee an opportunity to meet its responsibility not only because of the effect of the program upon the condition of the Government bond market in the first instance but also its ultimate effect upon member banks.

The meeting recessed for lunch, and reconvened at 3:00 p.m. with the same attendance as at the morning session except that Chairman Eccles and Mr. McKee were not in attendance.

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the Federal Open Market Committee held on February 28 and March 1, 1938, were approved.

Upon motion duly made and seconded, and by unanimous vote, the actions of the executive committee of the Federal Open Market Committee as set forth in the minutes of the meeting of the executive committee on February 28 and March 1, 1938, were approved, ratified and confirmed.

Mr. Burgess reviewed the operations which had taken place in the system open market account since the last meeting of the Federal Open Market Committee, including the sales of bonds and replacements by bills and notes during the recent period, which had resulted in a reduction of the bond holdings in the account with maturities in excess of five years to approximately $600,000,000.

Upon motion duly made and seconded, and by unanimous vote, the transactions in the system open market account since February 28, 1938, up to the close of the market today, were approved, ratified and confirmed.

At the request of the Committee for his views regarding the situation discussed by the Committee, Mr. Goldenweiser stated that approximately $4,000,000,000 in excess reserves might be expected before the end of the year, that this amount is larger than in 1936 when the Board increased reserve requirements, but that the situation had changed materially from the boom conditions that existed at that time to a condition of depression the end of which was not yet in sight. He expressed the opinion that the large amount of excess reserves would have the effect of reducing going rates on Government securities possibly to a no-yield basis on bills, to 1/4% to 1/2% on notes, and to 2% on bonds, and that, in these circumstances, the reduction of the system portfolio in an attempt to maintain rates would be a futile gesture which might deprive the system of its earning assets without accomplishing any useful purpose. Under these circumstances, and in the light of the determination of the Treasury to retire maturing bills, he felt that the system portfolio should be retained without making shifts to influence the market until such time as the securities purchased to replace maturing securities reach a no-yield basis. He thought it was clear that the system could not be expected to purchase replacement securities at a premium. He added that in his opinion the course to be followed was essentially one of inaction, that everything that could be done in the monetary field had been done, and that the system should stand by and determine on the basis of future developments what further action might be required.

Following Mr. Goldenweiser's statement there was a further discussion of the question whether, if the system takes no action to influence market conditions during the period of advancing prices, it should take such action during a period of market decline and it was stated by some of the members of the Committee that, regardless of the desire of the system to influence the market in the present situation and regardless of the policy followed in a period of market decline, the system was without the necessary power to prevent a decline in security yields at the present time and that, therefore, no purpose would be served in reducing the system portfolio even though it might be felt that under ordinary conditions the system had some responsibility to act.

At this point Chairman Eccles returned to the meeting.

He stated that he had just returned from a very thorough discussion of the entire problem with the Secretary of the Treasury and that, after reviewing the whole subject, pointing out the problem before the Federal Open Market Committee, recognizing the Treasury situation and recognizing that both the Treasury and the Board were in a very difficult position, there was not the slightest disagreement as to the essential facts of the situation. Chairman Eccles said that he had advised the Secretary that the Federal Open Market Committee had not decided on the course that it should take because it did not know exactly what program would be followed by the Treasury. He also said he had reviewed, for the information of the Secretary, the discussions which the Committee had had and that the Secretary understood the position in which the Committee was placed.

Chairman Eccles then stated that the Secretary had outlined quite fully the Administration conferences that had taken place at which it had been recognized that if the Treasury retired maturing bills it would create a difficult problem for the Federal Reserve System for the reason that there would be fewer bills in the market which could be used for replacement purposes, that the retirement of bills at the present time in addition to the effort of the Federal Reserve System to replace maturing securities would very likely put the Government securities market up when it was felt that it was already high enough, if not too high, and that this might have an adverse effect at a subsequent time. Notwithstanding these considerations, Chairman Eccles said, it was decided during the conferences referred to that the proceeds of the desterilized gold should be put into the banking situation, that this could be done more rapidly by paying off $50,000,000 of bills a week between now and June, and that, therefore, an announcement should be made that until further notice the Treasury would sell $50,000,000 of bills weekly. The Secretary stated, Mr. Eccles said, that it was too late to do anything to change that position this week, because telegraphic advices had already been sent to the Federal reserve banks that only $50,000,000 of bills would be offered next week. Mr. Eccles added that the Secretary felt that the press announcement would leave the Treasury free to change its policy during the succeeding week if it desired to do so. Chairman Eccles stated further that the Secretary had given assurance that, if the System desired, the entire matter would be considered again next week in the light of intervening developments.

Chairman Eccles' statement was followed by a consideration of the availability of bankers acceptances and other eligible securities in addition to Government obligations for purchase for the system account. There was also a discussion of the extent of the authority which should be given to the executive committee to effect transactions in the system account pending another meeting of the Committee.

At 5:05 p.m. Mr. Williams, who had not attended the meeting because of illness, entered the room.

There was a discussion of the question how far the Committee should permit the amount of bonds held in the System account to be reduced. Some members expressed the view that it should not go below $500,000,000 in present circumstances; that it might very well be maintained at the present level; but that the executive committee should have some authority to let bills run off without replacement. Following this discussion the Chairman stated that he would like to have the record show that the Committee had adopted a policy of not letting the portfolio run off unless a condition developed which would make it unreasonable to expect the system to replace its maturing bills; that the situation might change considerably during the next two or three weeks; and therefore that it would be advisable to review the matter with the Secretary of the Treasury again next week.

At 5:30 p.m. the meeting recessed with the understanding that it would reconvene on Friday, April 22, at 10:30 a.m.

Chester Morrill
Secretary.

Approved: M S Eccles
Chairman.

The meeting of the Federal Open Market Committee was reconvened in the offices of the Board of Governors of the Federal Reserve System in Washington on Friday, April 22, 1938, at 10:35 a.m.

PRESENT: Mr. Harrison, Vice Chairman
Mr. Szymczak
Mr. McKee
Mr. Ransom
Mr. Davis
Mr. Draper
Mr. Sinclair
Mr. Newton
Mr. Schaller
Mr. Peyton

Mr. Morrill, Secretary
Mr. Wyatt, General Counsel
Mr. Goldenweiser, Economist
Mr. Dreibelbis, Assistant General Counsel
Mr. Thurston, Special Assistant to the Chairman of the Board of Governors

Mr. Ransom referred to the fact that since action was taken by the Federal Open Market Committee at its meeting on March 1 in appointing Messrs. McKee and Ransom as alternates for Messrs. Eccles, Szymczak and Davis as members of the executive committee of the Federal Open Market Committee Mr. Draper had been appointed a member of the Board.

Thereupon Mr. Ransom moved that Mr. Draper be selected as the first alternate for members of the Board on the executive committee so that the alternates for such members of the executive committee would serve in the following order:

Mr. Draper
Mr. McKee
Mr. Ransom

Having been duly seconded, Mr. Ransom's motion was put by the chair and carried unanimously.

Mr. Harrison stated that, in view of the discussions at the meeting yesterday, he had instructed Mr. Burgess, Manager of the System open market account who had returned to New York following the meeting yesterday, to effect no transactions in the system open market account today until further instructions were received from the Committee, that the market at the present time was from 4/32's to 5/32's higher than yesterday's closing prices, and that if, in these circumstances, the Committee felt that Mr. Burgess should be given different instructions it was suggested that the Committee determine the instructions that should be issued.

Upon motion duly made and seconded, and by unanimous vote, the instructions given by Mr. Harrison to Mr. Burgess were approved, ratified and confirmed.

Mr. Harrison then presented the following resolution and moved that it be adopted. Mr. Harrison's motion was duly seconded:

In view of the fact that the present and prospective amounts of excess reserves of member banks are tending to make it more difficult for the System, by means of shifts in the maturities in the open market account, to exercise its influence towards orderliness in the Government securities market

VOTED that, until otherwise authorized or directed by the Committee, and in addition to the authority to make shifts in the maturities in the system open market account, the executive committee be authorized to permit fluctuations in the total amount of the account in order more effectively, with the means available and in the light of current conditions, to exert its influence towards orderly conditions in the Government bond market, provided, however, that the account shall not be increased or decreased by more than $200,000,000 from the present level of the account.

At Mr. Ransom's request, the following draft of resolution was read:

In view of the fact that actions of the Treasury and the Board of Governors in pursuance of the program recently adopted by the Government for the encouragement of business recovery have resulted in the creation of a large volume of actual and prospective excess reserves; and of the further fact that these actions have entirely changed the situation in the money market, it is the judgment of the Federal Open Market Committee that interest rates and bond yields should be permitted to adjust to the new conditions. Consequently, it is

VOTED that the executive committee is directed to maintain the system's open market account at its present level until the next meeting of the Federal Open Market Committee, except that, in case it becomes impossible to replace maturities in the account with other securities having a maturity not exceeding two years without paying a premium above a no-yield basis, the executive committee is authorized to permit the account to fall below its present level by an amount not exceeding $________.

After some consideration of the differences between the two resolutions further discussion thereof was deferred until Chairman Eccles, who was necessarily absent at the beginning of this session, could join the meeting.

Reference was made to the action of the Committee on March 1 in appointing a committee (Messrs. Davis, Ransom and Sinclair) to consider section 6 of Article I of the by-laws of the Federal Open Market Committee and to submit a report and recommendation, and it was stated that the committee was not prepared to submit a report at this time.

It was voted unanimously to request the committee to continue its study of the matter.

Reference was also made to the understanding at the last meeting of the Committee that Mr. Williams, Associate Economist, would submit a second memorandum which would be in the nature of a supplement to the memorandum submitted by him relating to the question whether the raising of reserve requirements caused the depression. It was stated that Mr. Williams was absent from this meeting because of illness and that the memorandum was not available at this time.

Mr. Harrison reviewed, for the information of Mr. McKee, who was not present at the afternoon session yesterday, the substance of Chairman Eccles' report of his discussion during the afternoon with the Secretary of the Treasury.

Chairman Eccles joined the meeting at this point and Mr. Harrison advised him of the instructions which he had given to Mr. Burgess and which had been approved by the other members of the Committee. Chairman Eccles stated that he concurred in the action of the Committee.

Mr. Harrison advised the Committee from time to time of the reports which he was receiving from the Federal Reserve Bank of New York regarding developments in the Government securities market.

The discussion of the problem before the Committee proceeded along the lines of analysis of the existing situation and of points brought out in the consideration of the problem during the preceding session.

Mr. Harrison said that he would like to have a vote upon his resolution, believing that it would be inadvisable for the Committee to decide at this time that it had no responsibility with respect to the money market or that it would witness a continued and rapid rise in the Government bond market without any action on its part in the direction of maintaining an orderly market, since government bond prices were almost at record heights with many issues selling on a no-yield basis, and present and prospective amounts of excess reserves were tending to force the market still higher, thus making it more vulnerable for attack in the future. In the event of a reaction later, he said, the Committee, no doubt, would decide to intervene not only because it had been its policy to exert its influence toward maintaining an orderly market on the decline, but also because it might feel some measure of responsibility for the condition of its member banks. He added that he felt that, in all the circumstances, the executive committee should at least have authority to permit some flexibility in the account if that should seem desirable as a factor in restraining a disorderly rise in the market. In his opinion, some reasonable reduction in the account at such a time could not properly be interpreted as a reversal of the policy of the Government with respect to excess reserves and probably would serve to make the market less vulnerable in the future.

Mr. Davis said that he would be opposed to any statement by way of preamble or otherwise that would indicate that the Committee under present conditions had any responsibility for the movement of the bond market or that would imply a criticism of actions which had been taken.

Chairman Eccles said that he could not vote for any resolution that implied a responsibility for maintaining an orderly market, which he felt could not be met under the conditions with which the Committee was confronted but that he would like to see the executive committee instructed to replace the maturing bills in the portfolio with bills to the extent that they could be purchased without paying a premium over a no-yield basis, letting that resolution stand from week to week pending another meeting of the full Committee to consider a change of policy.

During the course of the discussion Mr. McKee moved as a substitute for Mr. Harrison's motion that the executive committee be instructed to direct the replacement of the next maturing Treasury bills in the system open market account with Treasury bills or notes having maturities not to exceed two years provided that such securities could be purchased without paying a premium above a no-yield basis.

Mr. McKee's motion was duly seconded.

Mr. McKee stated that his motion was made with the idea that another meeting of the Committee should be held next week in order that the situation might be reviewed again.

At the conclusion of the discussion Mr. McKee's motion was put by the chair and carried unanimously.

Upon motion duly made and seconded, it was voted unanimously that another meeting of the Committee should be called to convene in Washington on Friday, April 29, 1938, at 10:30 a.m.

Upon motion duly made and seconded, and by unanimous vote, the Committee instructed the executive committee, until otherwise instructed by the Committee and subject to the limitations contained in the motion previously adopted on this date with respect to the next maturing Treasury bills in the account, to direct the replacement of maturing securities in the system open market account with other Government securities and to make such shifts between maturities in the account as may be necessary in the proper administration of the account, provided, that the amount of securities maturing within two years be maintained at not less than $1,000,000,000 and that the amount of bonds having maturities in excess of five years be not over $850,000,000 nor less than $500,000,000.

Upon motion duly made and seconded, and by unanimous vote, the Committee authorized the executive committee to permit such fluctuations within reasonable limits in the amount of holdings of Government securities in the system open market account between weekly statement dates as may be desirable for the practical administration of the account in making shifts between and replacements of securities pursuant to the general authority granted by the Federal Open Market Committee.

In taking these actions it was understood that the resolution adopted at the last meeting relating to an increase or decrease in the system account would be treated as being no longer in effect.

Thereupon the meeting adjourned.

Chester Morrill
Secretary.

Approved: M S Eccles
Chairman.