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 Saturday, September 27, 1941, at 10:05 a.m.

PRESENT: Mr. Eccles, Chairman
Mr. Sproul, Vice Chairman
Mr. Szymczak
Mr. McKee
Mr. Ransom
Mr. Draper
Mr. Fleming
Mr. Leach
Mr. Davis
Mr. Peyton

Mr. Morrill, Secretary
Mr. Carpenter, Assistant Secretary
Mr. Wyatt, General Counsel
Mr. Goldenweiser, Economist
Mr. Williams, Associate Economist
Mr. Dreibelbis, Assistant General Counsel
Mr. Rouse, Manager of the System Open Market Account
Mr. Piser, Senior Economist in the Division of Research and Statistics of the Board of Governors

Messrs. Roy A. Young, Alfred H. Williams, C. S. Young, Leedy, and Gilbert, alternate members of the Federal Open Market Committee

Messrs. McLarin and Day, Presidents of the Federal Reserve Banks of Atlanta and San Francisco, respectively

Mr. Clayton, Assistant to the Chairman
Mr. Thurston, Special Assistant to the Chairman
Mr. Sienkiewicz, Secretary of the Presidents' Conference

Mr. Morrill stated that Mr. Leedy had been appointed and had assumed his duties as President of the Federal Reserve Bank of Kansas

City, that in February of this year the Federal Reserve Banks of Minneapolis, Kansas City, and San Francisco elected the President of the Kansas City Bank, when appointed, as an alternate to Mr. Peyton as a member of the Federal Open Market Committee, that a record had been received of the election of Alfred H. Williams to serve as an alternate to Mr. Fleming as a member of the Federal Open Market Committee, and that it was the opinion of counsel that Messrs. Williams and Leedy were qualified to take the oath of office and assume their duties as alternate members of the Committee.

> Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the Federal Open Market Committee held on June 10, 1941, were approved.
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> 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 June 10, 1941, were approved, ratified and confirmed.

Those present were then furnished with copies of a report prepared at the Federal Reserve Bank of New York relating to the System open market account and the Government security market. Mr. Rouse reviewed the important points in the report and stated that there were no transactions in the account since the last meeting of the Committee so that the usual action with respect to the ratification of transactions in the account would not be necessary. He also stated that, in connection with the October first reallocation of securities in the

System account, some study had been given to the earnings and expenses of the Federal Reserve Banks for the current year and that from the estimates that had been made it appeared that total expenses would exceed earnings by approximately $500,000 which would be offset by profits of $504,000 realized from sales from the System account during the year.

Mr. Szymczak read a memorandum dated September 26, 1941, from Mr. Smead with respect to the earnings and expenses of the Federal Reserve Banks during 1941, which was in substantial agreement with the comments made by Mr. Rouse, and Mr. Szymczak stated that the memorandum would be checked and copies thereof furnished to the Presidents before they left Washington. A copy of the memorandum has been placed in the files of the Federal Open Market Committee. It was understood that the question of the earnings and expenses of the Federal Reserve Banks would receive consideration by the Presidents of the Federal Reserve Banks in their separate conference which would be held following this meeting.

> Upon motion duly made and seconded, the report submitted by Mr. Rouse was accepted and ordered filed.

Chairman Eccles stated that, before the reports of Messrs. Goldenweiser and John H. Williams and the consideration of open market policy, he would like to suggest that Mr. Ransom make a statement with respect to the discussions at the Treasury relating to action on reserve requirements and the subject of Treasury financing.

Mr. Ransom reviewed the discussions which he and Mr. Goldenweiser had had with representatives of the Treasury which culminated in action by the Board on September 23, 1941, to increase reserve requirements of member banks to the maximum of the Board's authority and the issuance of a joint statement by Chairman Eccles and the Secretary of the Treasury with respect to the granting of further authority over bank reserves to the Board of Governors. Mr. Ransom concluded his statement with a suggestion that it would be helpful, in further discussions which were to be had with the Treasury, if the Presidents would adopt some statement with respect to the desirability of having a pattern of rates for the financing of the defense program and which the monetary authorities would support by such measures as might be necessary, including open market operations by the Federal Reserve System. A copy of the substance of Mr. Ransom's statement has been placed in the files of the Federal Open Market Committee.

In a discussion of what might be regarded as reasonable rates at which Treasury financing could be done, Mr. Ransom referred to the steady decline in rates that had occurred during recent years and stated that he had expressed the opinion in the discussions with the Treasury representatives that it was extremely important that a policy be adopted which would put a floor under interest rates in order to prevent their decline to a point which would bring disastrous results. He also said that he felt the question of the broader application of selective credit controls should be faced and disposed of.

Mr. Sproul stated that it had been contemplated that before final action was taken by the Board to increase reserve requirements a meeting of the Federal Open Market Committee and the Presidents of Federal Reserve Banks would be held for the purpose of discussing the matter with them, but that circumstances arose, including the appearance of the Secretary of the Treasury at hearings on the price control bill, which made it necessary for the Board to take action on September 23.

Messrs. Goldenweiser and Williams were then called upon for statements with respect to the present business and credit situation.

Mr. Goldenweiser, after stating that copies of the review of the month which would appear in the Federal Reserve Bulletin for October and would contain a review of current developments in industry and agriculture would be furnished to those present, referred briefly to the developments which he said clearly indicated the existence of an inflationary situation at the present time and the need for further action to fight inflation.

He addressed the remainder of his remarks to some of the problems arising in connection with Treasury financing. According to estimates now available, during the rest of this fiscal year and the fiscal year 1943, the Treasury would have to borrow approximately $30,000,000,000 ($13,500,000,000 in fiscal 1942 and $16,500,000,000 in fiscal 1943) and, if nothing more were done than was being done at present to sell Government securities to others than banks, the banks would probably take not less than $15,000,000,000 of this total. The expansion in bank deposits that would take place, he said, raised acutely the question as to the desirability of further powers over reserve requirements and as to the kind of financing that should be done by the Treasury. He stated that the heart of the problem was the rates of interest at which the Treasury would borrow, that interest rates had declined to a record low level, but that, in view of the growing demand for funds by the Government and industry and the decrease in the supply of funds due to growth of currency in excess of gold imports, there would probably be no further decline, but a firming tendency. On the other hand, there was no reason to expect a general or substantial rise in rates.

He suggested that the alternative courses of action before the System were: (1) To do nothing and let the market rise or fall as it saw fit, which he thought was not a policy that should be seriously considered. (2) To continue the policy that had been pursued during the last three or four years of attempting to maintain orderly market conditions, which implied an underlying conception of a natural market, a conception which he said did not accord with conditions as they exist today. In his opinion the orderly market policy was about as much out of line with reality now as discount rate policy had become some years ago.

(3) In the event additional powers were obtained, to proceed to tighten credit controls to a point where excess reserves would almost entirely disappear, a substantial number of banks would be short of funds, and interest rates would be allowed to rise. Such a policy would have to be on the theory that higher interest rates were cheap insurance against inflation. In present circumstances this would not be a feasible policy for the reason that it would increase the cost of Government borrowing without being effective in preventing price rises, and it could not be carried out with the approval of other agencies of Government. It would also raise serious problems about the decline in the capital value of outstanding securities. (4) To adopt a policy under which a pattern of interest rates would be agreed upon from time to time and the System would be pledged to support that pattern for a definite period. The pattern of rates would not need to provide for the same range of fluctuation on all types of rates. It might limit fluctuations on long-term rates to a narrow range, and permit intermediate and short-term rates to respond more freely to current market influences. This appeared to him to be the wisest and most practicable policy at this time.

He commented that the problem presented by the suggestion of a pattern of rates was whether it was possible effectively to combat inflation without having rates rise more substantially than would be contemplated by the pattern, that there were differences of opinion on that point, but that he felt that rates probably would not go up materially in view of the existence of a large volume of funds and the growth of savings out of a rising income. The support that the System might need to give to the market would not be, in his opinion, on a scale that would offset such restrictive actions as the System might want to take.

Mr. Goldenweiser then referred briefly to the preferential rates established during the World War on the rediscount by Federal Reserve Banks of paper secured by Government securities, and expressed the opinion that in supporting a pattern of rates determined by the System and the Treasury in the present situation the System would be following the modern equivalent of that, and that the System would be well advised if it took that course.

He made the further statement that in any case it was the primary function of a central banking institution in time of war to contribute its major efforts toward meeting the needs of the Government, and that in his opinion the responsibility of the System in the field of credit control could be met, in so far as credit control could be effective in combating inflation, without interfering with its ability to stand by a pattern of rates agreed upon by the System and the Treasury.

At the conclusion of Mr. Goldenweiser's statement there were distributed copies of the review of the month for the October Federal Reserve Bulletin and memoranda dated September 26, 1941, from Miss

Gunhild Anderson of the Division of Research and Statistics of the Board of Governors on the estimated Treasury cash requirements for the fiscal years 1942 and 1943, and by Mr. Piser on the estimated distribution of the Government debt.

The meeting recessed and reconvened at 2:15 p.m. with the same attendance as at the morning session, and in addition, Mr. Thurston.

Mr. Williams expressed the opinion that the rise in industrial production would be less rapid than during the past year, and that there was some danger of unemployment resulting from a broad application of priorities, which indicated that the problem of fighting inflation was not one of taking all forms of anti-inflationary action that might be available, but rather a question of the determination of the character and the timing of the action to be taken. He pointed out that the System could attack the problem of inflation in only a limited way, that there were other fronts over which the System had no control, including agricultural prices and wages and on which little headway was being made, and that it was not possible to adopt an effective program which did not include effective policies with respect to these matters.

He felt that the Administration's tax program was progressing satisfactorily but that sufficient efforts had not been made to tap non-bank funds for the purchase of Government securities, that a great feel more could be done in that field, that that was a point on which the System in its further negotiations with the Treasury could press for consideration as having a bearing on the System's responsibilities, and that before the System could adopt an intelligent program with respect to what, if any, further credit restriction was needed, it would be necessary to ascertain to what extent Treasury needs could be met from non-banking funds and to agree on a financing program which would be attractive to non-banking investors.

In connection with references that had been made to what might be regarded as an artificial market, Mr. Williams expressed the opinion that it would be a mistake for the Federal Reserve System to create a situation in the Government security market which would make it appear that the market had to have continuous support as that eventually would cast doubt upon the public credit. He stated that something short of that should be considered, and that he felt that at this stage the System should devote itself to a policy which would contemplate (1) full cooperation with the Treasury in developing a program which would tap non-banking funds to the fullest possible extent, (2) exploration with the Treasury of the possibility of stabilizing interest rates, and (3) a study of the changes that should be made in the basis for determining reserve requirements, as the present was an excellent time to make such fundamental changes as would contribute to the stability of the money market.

On the question whether there should be a further reduction in excess reserves he felt that the important point was what the effect would be on the Government security market, that if excess reserves were going to be reduced in any event by currency withdrawals and an increase in bank loans and investments the rate of interest could not be expected to decline much further, that we could not avoid the conclusion that further increases in reserve requirements would increase interest rates and create a need for open market action that would not otherwise exist, and that before any action in that direction was taken we should examine the motives behind it.

Mr. Williams' statement was followed by a discussion of the possible effects of the Board's recent action to increase reserve requirements, the further steps that might be taken in the field of credit control, the place that selective credit controls might play in the picture, and what the immediate future policy of the Federal Open Market Committee might be.

Mr. Sproul stated that the immediate problem before the Committee was what action was to be taken with respect to open market operations, that in his opinion there would be further reactions in the market over the next few weeks to the increase in reserve requirements which might necessitate some action by the Open Market Committee, but that any transactions necessitated by that situation undoubtedly could be handled under existing authorities. Mr. Sproul also stated that he favored exploration with the Treasury of the possibility of determining upon a pattern of rates, that the present might be a desirable time to undertake such a program, but that no commitment should be made by the System to support such a pattern of rates without regard to what might be the financing policies of the Treasury, and that any agreement with respect to rates should be coupled with the adoption by the Treasury of a plan of financing designed to attract as many non-banking funds as possible.

Mr. Ransom stated that any program agreed upon should not be in the nature of an unconditional commitment by the System to maintain interest rates, but that it would not be possible to reach an agreement on the matter with the Treasury without some commitment on the part of the System that it would take action within its power to support the pattern of rates agreed upon.

Mr. Sproul suggested that arrangements be made to have a representative member of the Federal Open Market Committee participate in the further discussions with representatives of the Treasury, and there was unanimous agreement that that should be done.

There followed a discussion of various questions involved in the matters which were to be the subject of further consideration with the Treasury and of Mr. Ransom's suggestion that a statement be agreed upon with respect to a pattern of rates at which the financing of the defense program would be undertaken and which the monetary authorities would undertake to support by such measures within their power as might be necessary. It was the consensus that this suggestion was a matter which should be taken up at the meeting of the Presidents' Conference with the Board of Governors to be held tomorrow.

Consideration was then given to the authority to be granted to the Executive Committee to direct the execution of transactions in the System account and Mr. Sproul stated that, in his opinion, a renewal of existing authorities would be adequate to meet any situation that could be foreseen at the present time and that in the event further action became necessary another meeting of the Federal Open Market Committee should be called.

> Thereupon, upon motion duly made and seconded, the following resolution, which was in the same form as the resolution adopted at the meeting of the Committee on June 10, 1941, was adopted by unanimous vote:
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> That the executive committee be directed until otherwise directed by the Federal Open Market Committee to arrange for such transactions for the System open market account (including purchases, sales, exchanges, replacement of maturing securities, and letting maturities run off without replacement) as in its judgment from time to time may be advisable in the light of existing conditions; provided that the aggregate amount of securities held in the account at the close of this date shall not be increased or decreased by more than $200,000,000.

Mr. Morrill referred to the fact that under date of August 15, 1941, a letter was received from Under Secretary of the Treasury Bell stating that there was being published in the monthly Treasury Bulletin a tabulation showing the ownership, by issues, of direct and guaranteed obligations of the United States, that in this tabulation the securities held in the System account were included with securities held by investors other than banks and insurance companies and Government agencies and trust funds, and that authority was desired to include the System's holdings with the holdings of Government agencies and trust funds under the caption "Held by Government Agencies and Trust Funds and by Federal Reserve Banks". After conferring with Mr. Rouse, and with the approval of Chairman Eccles, Mr. Morrill sent a letter to Mr. Bell, on August 21, 1941, stating that there would be no objection to the publication of these figures in the manner indicated, with the understanding that separate figures showing the holdings of Government agencies and trust funds would not be released in some other connection in such manner as to make it possible by subtraction to determine the Federal Reserve Banks' holdings of individual outstanding issues, and that it would be preferable as long as the publication of the figures was continued in the form proposed, to continue the lag of approximately two months between the date as of which the figures were published and the release of the Treasury Bulletin.

The action of Chairman Eccles in authorizing the letter to Mr. Bell was approved and ratified by unanimous vote.

Thereupon the meeting adjourned.

Chester Morrill
Secretary.

Approved: M S Eccles
Chairman.