A meeting of the executive committee of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System in Washington on Friday, November 1, 1940, at 2:45 p.m.

PRESENT: Mr. Eccles, Chairman
Mr. Harrison, Vice Chairman
Mr. Szymczak
Mr. Davis
Mr. Sinclair

Mr. Morrill, Secretary
Mr. Carpenter, Assistant Secretary
Mr. Wyatt, General Counsel
Mr. Goldenweiser, 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

Mr. Draper, Member of the Federal Open Market Committee

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the executive committee of the Federal Open Market Committee held on September 27, 1940, were approved.

It was stated that on October 25, 1940, the members of the executive committee, under the authority of paragraph numbered 3 of the resolution adopted at the meeting of the committee on September 27, authorized the Federal Reserve Bank of New York to make such outright sales of securities from the System open market account as might be effected without adversely affecting the market provided that the total amount of securities in the account be not decreased through operations under paragraph numbered 2 of the resolution adopted at the meeting of the committee on September 27, by more than $100,000,000 in addition to the authority already granted by that paragraph; the reason for the additional authority being that through October 25 the Bank sold $89,900,000 of securities and it was believed desirable, in the light of the resolution adopted at the meeting of the Federal Open Market Committee at its last meeting, to grant the additional authority to make sales from the account.

> Upon motion duly made and seconded, and by unanimous vote, the action of the members of the executive committee in granting additional authority to the New York Bank was approved, ratified and confirmed.

Mr. Rouse reported briefly on the transactions which had been effected in the System open market account since the last meeting of the executive committee as set forth in a report of open market operations prepared by him for this meeting and filed with the Secretary during the meeting. The report covered operations through October 30, 1940, and Mr. Rouse stated there were no transactions in the account yesterday.

> Upon motion duly made and seconded, and by unanimous vote, the transactions in the System open market account for the period since that covered by similar action taken by the executive committee on September 27, 1940, to and including October 31, 1940, were approved, ratified and confirmed.

There ensued a discussion of the directions to be issued to the New York Bank with respect to transactions in the System account and it was suggested that the authority given at the last meeting of the committee be renewed.

Thereupon, upon motion duly made and seconded, and by unanimous vote, the executive committee directed the Federal Reserve Bank of New York, until otherwise directed by the executive committee,

(1) To make such shifts of securities in the account (which may be accomplished when desirable through replacement of maturing securities) as may be necessary in the practical administration of the account or for the purpose of exercising an influence toward maintaining orderly market conditions, up to an aggregate of $200,000,000 of purchases and a like amount of sales or redemptions, provided that in making such shifts the total amount of bonds held in the account be not increased or decreased by more than $100,000,000;

(2) To make such outright purchases for the System account as may be necessary for the purpose of exercising an influence toward maintaining orderly market conditions, or, when market conditions permit, to make such outright sales as may be effected without adversely affecting the market, provided that the total amount of securities in the account be not increased or decreased through operations under this paragraph by more than $100,000,000; and

(3) Upon approval by a majority of the members of the executive committee, which may be obtained by telephone, telegraph, or mail, to make such other shifts or such purchases or sales (which would include authority to allow maturities to run off without replacement) for the account as may be found to be desirable within the limits of the authority granted to the executive committee by the Federal Open Market Committee.

Chairman Eccles said there were two aspects of the procedure with respect to the sales which had been made during the last month which he would like to discuss. One was that, while sales were made from the account in substantial amounts for the purpose of reducing the account at a time when there was sufficient strength in the market to absorb the sales without adversely affecting the market, because of the relatively small advance in prices during the period of the sales it might have been said that the System was pegging the market, and that he would like to feel that, if the market were to become relatively as low as it was now relatively high, the executive committee would be willing to purchase securities as readily as it sold them during the last month, without objection on the ground that the committee would be attempting to peg the market. He said that in his opinion it was not only a question of exercising a stabilizing influence but also of recognizing the time when purchases should be made, with the understanding that they could be made to the same extent as sales are now being made, so that there would be securities in the portfolio which could be sold in a period of disorderly market advance. He added he could foresee a situation, after a substantial decline in the market, when the System should purchase a considerable amount of securities although the market might be moving in a very narrow range.

In a discussion of this question, Mr. Harrison concurred in the latter point referred to by the Chairman but suggested that sales of securities at a time when they could be absorbed without adversely affecting the market probably would not be a satisfactory measure of the purchases that should be made when the market was declining, and that when another period of serious market weakness occurred, the committee might be faced with an entirely different set of circumstances which would require a different procedure from that called for in any period in the past.

Mr. Davis said that the extent to which the System would be willing to buy securities in a period of market weakness might be affected by the amount of securities sold during times of market strength. Other members of the committee indicated agreement that this would be the case at least psychologically.

Chairman Eccles then said his second question was whether the System should continue to sell securities until the portfolio was reduced to approximately the maintenance point, that is, to the point where the earnings of the System would be only sufficient to meet its expenses, or whether there should be retained in the account sufficient securities above that point so that the System would be able to sell securities in the event enabling legislation were enacted and excess reserves were reduced, say to $500,000,000, and it was desired to effect a further reduction in excess reserves through open market operations to counteract inflationary developments. He doubted whether a situation would exist for some time in the future in which the Federal Reserve System would have substantial earnings from discounts for member banks and in these circumstances he questioned whether the System should reduce its portfolio to the maintenance level.

Mr. Sinclair raised the question whether the committee should take the position that it would not, for market reasons, reduce the System's holdings of securities below the maintenance level and Chairman Eccles replied that he felt it would be a desirable thing for it to become recognized that the System regarded a portion of its portfolio as necessary for earnings and not available for the purposes of credit control.

Mr. Harrison stated that in the event of an inflation requiring sales of securities from the account he would be willing to go below the maintenance level for the reason that, while it is important that the Federal Reserve Banks meet their expenses, it is not important that that be done in any particular year. He also said that, should it be necessary to reduce the System account below the maintenance level, the System should undertake to reduce the free services to member banks, that he felt the System was rendering services at the present time that should be paid for by the banks or their customers, and that if the question of expenses were involved he did not think the System would be justified in taking the position that it would not, for reasons of credit control, reduce the portfolio below the maintenance level and at the same time do nothing to reduce the expenses of the System.

Chairman Eccles suggested that if such a situation should occur it would have become necessary to increase reserve requirements and, perhaps, Federal Reserve Bank discount rates which would tend to drive banks out of the System and if, at such a time, charges for services rendered by the Reserve Banks to member banks were increased it would only aggravate that tendency, so that before these actions would be wholly effective it would be necessary to bring about a greater degree of uniformity in the banking system.

In a further discussion, Mr. Harrison stated that if the System account were further reduced at this time there would be further profits from sales which would, to some extent at least, offset the need for earnings, and that while he saw some advantage in keeping some amount of securities in the account above the maintenance level he would have no hesitation at this time in reducing the portfolio to around that level, feeling that there would be occasion for further purchases before it would be necessary to sell securities for the purpose of credit control.

Mr. Harrison then suggested that it be understood that the New York Bank would continue to operate in the account substantially as it had done during the past month with the further understanding, however, that a meeting of the Federal Open Market Committee would be held some time during the early part of December when the entire matter would be reviewed.

In response to an inquiry from Mr. Davis whether the New York Bank would continue to sell securities in the event the market began to decline, Mr. Harrison replied in the negative and Mr. Rouse stated that should there be a decline followed by a resumption of the upward movement, the Bank would resume selling on the rise from the low point.

At the conclusion of the discussion, the suggestion made by Mr. Harrison with respect to continued sales from the account was agreed to pending a meeting of the full Committee in early December.

Mr. Rouse referred to the suggestion made at the meeting of the Federal Open Market Committee on September 27, 1940, that an effort be made to dispose of some of the System's holdings of the March 1941 notes so as to relieve the portfolio, to the extent of such sales, of the necessity for exchanging the maturing notes for a new issue of Treasury obligations. Mr. Rouse stated that approximately $95,000,000 of the notes were still held in the account and that if they were sold the total volume of sales might be somewhat larger than otherwise would be the case and that in the disposition of these securities it might be found desirable to shift some of them into other issues as opportunity afforded and subsequently to sell the acquired issues. No objection was interposed to the procedure suggested by Mr. Rouse in this connection.

Thereupon the meeting adjourned.

Chester Morrill
Secretary.

Approved: M S Eccles
Chairman.