

Competition
With Member
Banks

It may be agreed that open-market operations on occasions are competitive with member banks but the limitations upon the reserve banks' open-market powers serve to soften some of the objections which otherwise might be made against their utilization. If in adding funds to or withdrawing them from business use through open-market operations the reserve banks could disregard the special requirements of the bill market and if they were under no obligation to heed the direction and volume of gold flows, there might be decided objection to bestowing such powers upon the reserve banks. As it is, however, the reserve banks' open-market powers are usually of limited influence only, but they are important in that they serve to increase the effectiveness of other powers.

Government
Securities

The bulk of open-market transactions are in government securities and bankers' acceptances. The maintenance of a discount market for foreign bills in New York, and the necessity of support of an incompletely understood type of bill—the acceptance—require at times that rates of acceptances be fixed with a view to considerations other than the use of the acceptance as a credit volume control. It is essential, therefore, that there be some asset of unquestioned value available in substantial supply, which can be dealt in by reserve banks. Fortunately government securities, especially short-term Treasury Certificates, have met these tests. Without the right to buy and sell governments, reserve banks would be unable to exercise any adequate control over the volume of reserve credit.

Recommendation

The Committee recommends that the present powers of the reserve banks to engage in open-market operations should be continued.

Note Issues

In the early days of the banking reform movement remedial plans frequently were centered upon changes in note issue provisions. This emphasis upon note issue was due in large part to the fact that the cause of each major disturbance was manifested superficially by a shortage of currency and attention was concentrated upon this rather than upon the credit developments which may have been responsible for the currency strain. Since, furthermore, the provision of currency was generally regarded as a government function, reform plans were careful to specify that the central institution's notes should be issued only under certain clearly indicated conditions. In the original Reserve Act attempt was made to emphasize the special serviceability of the new system to commerce and agriculture by providing that reserve notes should be issued only against the collateral of paper obtained by rediscounting.

Original
Provisions of
Law

Supply of Credit
Not Collateral,
Is Critical
Factor

The main consideration, however, as experience has shown, is not the collateral, but the character of operations member banks are encouraged to engage in and the adequacy of the mass of credit

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