

Benjamin Strong
Governor, October 1914 to October 1928

The Federal Reserve was established on short notice immediately after the start of World War I. In this, his earliest address as Governor of the Federal Reserve Bank of New York, Strong describes the activities of the Bank in its first seven months. He explains the steps taken to ensure that the Federal Reserve would have sufficient resources to meet bank runs and the measures adopted to establish a check clearing system for member banks.

The Formation of the Federal Reserve System by Benjamin Strong

This is the first general convention of the bankers of the State of New York since the establishment of the Federal Reserve System, and, therefore, the first opportunity to address all of the bankers of the state in regard to the work which has been done by the Federal Reserve Bank and in regard to some of the larger aspects of the system. Your president has asked me to refer to our plan for collecting checks and to the new regulation regarding state banks, but I want first to briefly review some of the work that has been accomplished by the Bank since its organization last November.

On October 26, 1914, it was decided by the Secretary of the Treasury that the situation brought about by the war in Europe necessitated the immediate organization of the Reserve Banks, and November 16 was

fixed as the date when they should open for business. On November 2, \$3,321,950 of gold was received from the member banks of this district in payment of the first installment of our capital. On the morning of the 16th of November, an organization, largely temporary, consisting of seven officers and 85 clerks had been assembled, and on that day \$99,611,670 of reserves were transferred to the Bank by the member banks. We had been successful in renting satisfactory offices already equipped with the furniture and fixtures necessary for our accommodation. Our temporary organization has since been gradually converted into a permanent organization, consisting now of five officers and 52 clerks, including stenographers, messengers, watchmen, and porters.

Two additional installments of capital have been received, making the present paid-in capital \$9,961,650, being 50 percent of the statutory amount. Reciprocal accounts have been established with the

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other 11 Reserve Banks for the purpose of handling interbank transactions, such as collections and investments. Through these accounts, the Federal Reserve Bank of New York has up to this time handled \$426,300,000 of exchange and \$25,000,000 of currency shipped to us to create exchange. Balances have fluctuated widely, the net amount due the New York bank at times exceeding \$20,000,000. On May 19, 1915, for the purpose of facilitating prompt settlement of these balances at minimum cost, there was deposited in Washington by all the Reserve Banks, and placed under the control of the Federal Reserve Board, a fund of gold sufficient to enable them to effect settlements between themselves without transferring any currency and simply by exchange of telegraphic advice. These settlements are at present made weekly, but if a larger volume of transactions makes it necessary, the fund can be increased and the settlement effected daily.

After some months of study by the Federal Reserve Board and the officers of all the Reserve Banks, the Federal Reserve Bank of New York, in common with the other banks, has taken the first step toward the creation of machinery for collecting checks for its member banks within its own district. Plans for establishing a system of bank transfers have been agreed upon by all 12 of the Reserve Banks and will shortly be placed at the disposal of the member banks, to enable them to effect prompt and economical transfers to all parts of the country. This system will be gradually developed and enlarged. Service of this character is made possible largely through the establishment of the Gold Fund in Washington, by means of which balances between the Reserve Banks created as a result of these transfers will also be settled.

In the first seven months of our business the New York Reserve Bank has discounted for its member banks 1,501 notes, amounting to \$8,284,349.70. It has also purchased in the open market 387 acceptances of a total value of \$9,315,158, and it has made 41 investments in short time municipal warrants of a total value of \$11,160,000. In addition to the investments made for its own account, it has purchased \$23,697,508.93 of acceptances and municipal warrants for account of eight of the other Reserve Banks, on their instructions.

From these discounts and investments, the Bank has to date made gross earnings of \$158,710.38, its current expenses have been \$116,948.84, leaving \$41,761.54 of net earnings, which will be applied to organization expenses amounting to \$181,654.36. These are partly made up of the cost of initial purchases of necessary supplies and fixtures, and making changes in our office. \$35,424.18 however, consists of the assessments levied against the banks for its proportion of the

expenses of the Federal Reserve Board and \$98,180.98 represents the actual cost of preparing Federal Reserve notes issued and to be carried in stock. The directors of the Bank have authorized the preparation of a total of \$300,000,000 of notes of various denominations, determined by experience gathered from all sources available as to the demand for currency. This will involve a considerable outlay by the Bank, but the assurance to the member banks that we have on hand at all times not less than \$250,000,000 of currency available against emergencies, well justifies the cost. There is at present on hand over \$183,740,000 of notes and the supply is being increased so as to complete the amount in a few weeks. To this date there has been issued \$34,600,000 in denominations of \$5 to \$100 inclusive, of which amount \$34,420,000 now outstanding are covered by a like amount of gold deposited with the Federal Reserve Agent.

Of course, the ability of the Reserve Banks to increase their gold reserves, beyond the amount of the member banks' deposits, is dependent upon their ability to issue notes against deposits of gold. This process is now in successful operation, the New York bank alone having issued, as stated, \$34,920,000 of notes against a like amount of gold deposited with the Federal Reserve Agent, and all 12 of the Reserve Banks show \$58,291,000 of gold so held.

The New York Clearing House Association has admitted the Bank to limited membership, thereby giving us facilities for clearing checks without imposing liabilities which we are not authorized to assume; and in all matters pertaining to our organization and the development of our business, the clearing house has given us loyal cooperation. The work of the Bank is being carefully departmentalized under the direction of experienced men. Owing to the simplicity of the work to be performed and the machinery for handling it, I am confident that in due time the Bank will be more economically managed than any other bank of its size in the world. Simplified methods of bookkeeping, and permanent statistical records, are being studied and adopted without, however, attempting to burden the organization with unnecessary detail. Credit files have been started to record the condition of our member banks, as well as information gathered in regard to paper offered for discount by those banks which avail of our facilities. In time this record will be one of the Bank's most valuable assets, enabling it to promptly and safely meet unusual demands that may be made upon its members.

This brief review of the past seven months' work must not give the impression that it has been an easy task or accomplished without arduous labor. Everything pertaining to the organization has been new and

unried. It may be said that on October 26 the Bank's equipment consisted of little more than a printed copy of the Federal Reserve Act; whereas, today, it is a fully

equipped bank with an organization perfectly capable of meeting any emergency and is promptly transacting the business entrusted to its care.