



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

OFFICE OF THE CHAIRMAN

March 7, 1968.

The Honorable Del Clawson,
House of Representatives,
Washington, D. C. 20515.

Dear Mr. Clawson:

This is in reply to your request for comment on a proposal by Mr. Preston Martin, Savings and Loan Commissioner of the State of California, for possible Federal Reserve "backstopping" of the consolidated obligations of the Federal Home Loan Bank System. As you will recall, he requests the Federal Reserve to commit itself to buy FHL Bank obligations--either directly or in the secondary market--as a means of cushioning the impact of monetary policy on the savings and loan industry and housing during periods of "very severe" credit restraint.

At the outset it should be noted that Federal Reserve purchases of FHL Bank obligations directly from the FHLB System are not authorized under present law. Section 14(b)(2) of the Federal Reserve Act (12 U.S.C. 355), which was added to the law by the Act of September 21, 1966, provides that the Federal Reserve Banks may "buy and sell in the open market, under the direction and regulations of the Federal Open Market Committee, any obligation which is a direct obligation of, or fully guaranteed as to principal and interest by, any agency of the United States." Although the Reserve Banks are also authorized by section 14(b) of the Act to purchase certain obligations of the United States directly from the Treasury, this authority does not extend to all agency issues but only to those which are fully guaranteed as to principal and interest by the United States. Moreover, since existing law already authorizes the Secretary of the Treasury to lend up to \$1 billion directly to the FHLB System, a similar authorization to the Federal Reserve would be simply additive.

While the 1966 act does authorize the Federal Reserve to purchase FHL Bank obligations in the open market, such buying is not really a feasible means of supporting the savings and loan industry. To have a significant influence on flows of funds to the FHLB System at times of severe credit squeeze, such Federal Reserve acquisitions would have to be very large and concentrated within a few months.