Thirtieth Annual Report

Federal Reserve Bank of New York

For the Year Ended December 31, 1944

Second Federal Reserve District

FEDERAL RESERVE BANK OF NEW YORK

March 12, 1945

To the Stockholders of the
Federal Reserve Bank of New York:

I am pleased to transmit herewith the thirtieth annual report of the Federal Reserve Bank of New York reviewing the year 1944.

ALLAN SPROUL,
President.

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WAR SERVICE

Members of the staff of the Federal Reserve Bank of New York are serving their country at war, both "in the service" and "on the job."

More than 800 men and women have joined the armed forces of the United States, one man is in the Canadian Army, 24 men are in the Merchant Marine, and two women are enlisted in the American Red Cross for foreign service. Ten men have lost their lives in the service of their country and in defense of our freedom.

This service and this sacrifice we can only repay, in some small measure, by seeing to it that our support of the war effort is unflagging. The efficiency with which the work of the bank has been carried forward during the past year has demonstrated that the members of the staff recognize this responsibility and have the will to discharge it.

ALLAN SPROUL,
President.

Federal Reserve Bank of New York
Thirtieth Annual Report

The year 1944 saw the American economy operating at its peak. Looking back, we can see that the great expansion of output since 1939 has divided into three phases, a strong upward movement to the end of 1941, an extraordinary upsurge in the next two years following Pearl Harbor and our entry into the war, and since the end of 1943 the creation of a high plateau.

The "gross national product" (the total dollar value of goods and services produced) was 199 billion dollars in 1944, compared with 188 billion in 1943, part of the increase being accounted for by a further rise in Government expenditures from 95 billion dollars to 99 billion, and the rest by a rise in output available for private use (mainly consumer goods and services) from 93 billion dollars to 99 billion. But the increase in the yearly totals represented the maintenance of the very high level already reached by the end of 1943 rather than any further expansion of output as a whole.

While broadly speaking, therefore, the year 1944 was one of maintenance of our war program rather than further growth, some of the changes that took place during the year throw further significant light upon the processes whereby our war effort is being directed with increasing effectiveness toward its objective, the winning of the war. Within the war program there has been a progressive shifting of emphasis from construction of plant and equipment to production of munitions and to the movement of men and munitions overseas. By the middle of 1943 the construction program was already passing its peak, and in 1944 expenditures for war construction declined by two thirds from the preceding year. But this decline was more than offset by the increase in expenditures for munitions and for the pay and subsistence of the armed forces. Among the major indices of our war effort last year, the production of munitions showed the largest gain. The fact appears to be, however, that by the end of 1943 the output of munitions had also reached its peak. Unlike 1942 and 1943, when pressure was being exerted generally to expand the production of war materiel, the year 1944 has been characterized as one of "selective pressure over a diminishing segment of the program." Where desired, the expansion achieved last year was large, though in some cases not up to the schedules set, and the net result was approximately to offset the decline in the much larger segment of the munitions program in which downward adjustments of production schedules occurred.

Meanwhile the movement overseas of combat materiel and all other goods needed to support our military operations and those of our Allies continued in 1944 to show a marked expansion over the preceding years. The number of cars unloaded for export was nearly one-third greater than the preceding year. Shipments from West Coast ports, mainly to Pacific theaters of military operations, have been stepped up at a relatively faster rate since the end of 1943 than have shipments from East Coast ports which are the main source of supply of the European offensive.

While these shifts in the character of our war effort were taking place, increasing attention was given last year to the problems of the postwar period. Within our special sphere of interest the outstanding event was the International Monetary and Financial Conference held last July at Bretton Woods. A later section of this report is devoted to the proposals for an International Monetary Fund and an International Bank for Reconstruction and Development now under consideration in Congress. Without anticipating that discussion, it can be said that the one point on which there seems to be general agreement, both here and abroad, is that the success of any measures for international cooperation will have to depend, more than on any other single factor, upon our success in maintaining high national income and employment. With the United States producing nearly half the world's manufactured goods and using about half the world's raw materials, international monetary and economic stability, by whatever means sought, will not be possible without stability at home.

But our domestic outlook was probably never more confusing than at present. So far as the war period is concerned, we have progressed far enough toward its end to have a reasonable certainty that there will be no major inflationary developments to disrupt the program. Broadly regarded, the behavior of prices has been good—much better than in the last war. Though diverse tendencies were apparent last year in commodity markets and there has lately been discussion of rising security and real estate prices, the official Bureau of Labor Statistics indexes of the cost of living and of wholesale prices showed relatively small changes from 1943. Apart from a broadening of rent controls to numerous critical areas, the administration of the price stabilization program was largely devoted to the policing of existing controls, taking care of loopholes and specific abuses, and making adjustments in ceilings designed to encourage production, to alleviate price-cost squeezes, or to curb excessive profits. Some upward adjustments in the wage scales of labor were permitted during 1944, but these adjustments were generally more moderate than those of the immediately preceding years.

The comparative stability of prices during the war is one of the most favorable factors bearing on the postwar period. Some other features of our wartime economy, however, raise difficult questions for the future. Last year was again characterized by financial and monetary expansion. The Federal debt rose another 62 billion dollars, commercial bank assets expanded more than 22 billion, and the money supply—the total of bank deposits and currency in circulation—was enlarged by an additional 28 billion. Though civilian consumption reached a new high peak, the volume of money incomes again exceeded consumption by a wide margin, and the liquid assets of individuals and of business again substantially increased. At the same time the deferred demand for consumer durable goods and presumably also for civilian capital goods not now available continues to pile up.

What these wartime facts portend for the postwar period is a complex question. Placed on top of an already high level of national income and employment, such as we have at present, such a volume of deferred demand for civilian goods and services, backed up by the large wartime savings* and the greatly expanded money supply, would indeed suggest postwar inflation; and it must be borne in mind, at any rate as a possibility, that any large-scale cashing-in of its holdings of Government securities by the public would force these securities into the banks and thus still further expand the supply of money. If such a wave of private expenditure should come before reconversion from war to peacetime production had gone far enough to match it with an expanding supply of goods, there might well develop a runaway rise of prices and all the other disorderly manifestations of an inflationary boom.

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* The accumulation of liquid assets by individuals and business organizations is discussed in a later section of this report, "The Debt and the Claims upon It."

There is at least enough plausibility in this kind of analysis of possible postwar developments to indicate the paramount necessity of maintaining wartime controls until we can be sure they are no longer needed. But in an over-all view the deflationary implications of our present situation may be more serious. The largest single fact about the postwar period is that there will be a huge decline in military expenditures. It will represent the greatest loss of market in our history. War expenditures will decline from some 80 billion dollars a year to perhaps 6 to 8 billion, and total Government expenditures (including State and local) will fall from over 100 billion dollars to perhaps 30 billion. Government deficits, now of the order of magnitude of 50 billion dollars a year, must be replaced, according to the ideas of many, by a balanced budget (or even by a surplus), while even those who stress the need of further Government expenditures to take the place of the present military program as a means of providing high employment, talk only of relatively modest deficits of perhaps 3 billion dollars a year. How to bring about such a change in Government finances and still provide jobs for all, or nearly all, will surely be one of our major postwar problems.

There is not space in this report to discuss this problem, or even to outline the diversity of views that are developing with regard to it. One important fact to bear in mind is that with the return to normal conditions it will not be necessary to maintain the wartime level of national income. A large part of what we now produce is not intended to serve any economic purpose, in the usual sense. By reconverting our resources to peacetime uses we can increase both our consumption and our capital equipment even though total production is declining; and by the resumption of a normal work-week and the voluntary withdrawal from employment of many women and old and young workers who would not normally be employed, we can considerably reduce the dimensions of the employment problem.

But whether such adjustments, by themselves, will be adequate to solve the problem, particularly after the wave of deferred demand has run its course, seems doubtful. If we are to attain, for example, such a level of postwar national income as the full-employment estimate of 140 billion dollars so widely used in current discussions, we shall need to have not only a great increase of private investment but (what is far more important in terms of comparative magnitudes) an expansion of consumption by at least 40 per cent beyond any level previously known in time of peace and substantially above the current (civilian) wartime level, which is the highest in our history. How this is to be brought about in ways consistent with the preservation of free enterprise, and what measures of cooperation between Government and business it will require are questions deserving the most intensive study.

No one wants to defer the final peace because the new problems it will bring will be hard, but it still seems probable that the war will end in two stages rather than abruptly. We should be able to take advantage of the interval between the end of the war in Europe and the end of the Pacific war not only to make a more orderly transition from a war to a peace economy but also to prepare ourselves for the much more fundamental long-run problems which appear to lie ahead.

Government Expenditures, Receipts, and Borrowings

During the calendar year just closed, total expenditures of the Federal Government* reached 96 billion dollars, a sum more than five times the total cost of financing the First World War. The increase over the preceding year came to 7 billion dollars, the difference being accounted for largely by a rise in war expenditures from 85 billion in 1943 to 91 billion in 1944. The excess of expenditures over net receipts was a little less than in 1943, 52 billion dollars compared with 55 billion, as tax and other revenues, which had more than doubled between 1942 and 1943, rose further in 1944 from 35 billion dollars to 44 billion. The continued growth of tax and other revenues was explained by the collection of individual income taxes on a current basis (which started the middle of the preceding year) and the payments due on March 15 of one half of the "unforgiven" portion of the individual income tax liabilities against 1942 or 1943 incomes; by higher rates provided for in the Revenue Act of 1943; and by the fact that incomes averaged somewhat higher during the year. The Individual Income Tax Act of 1944, enacted in May, was designed mainly to simplify the operation of the current tax payment principle for individual taxpayers.

Although the Government's need for borrowing was somewhat less than in 1943, the actual amount borrowed was somewhat more, 62 billion dollars in 1944 compared with 57 billion in 1943. As a result of the fact that the Sixth War Loan drive came at the end of the year, the general fund balance of the Treasury was at the high level of 22 billion dollars

* Includes net expenditures of Government trust funds and corporations except for debt retirement.

on December 31, 1944 compared with 12 billion a year earlier. Of the 62 billion dollar net increase in the Federal direct and guaranteed interest-bearing debt during 1944, about 32 billion dollars or 52 per cent was accounted for by additions to the holdings of individuals, corporations, and other nonbank investors (exclusive of Government agencies and trust funds); 5 billion or 8 per cent by additions to the holdings of Government agencies and trust funds; and about 25 billion or 40 per cent by additions to the holdings of commercial and Federal Reserve Banks. The net absorption of 32 billion dollars of Government securities by nonbank investors compares with 29 billion in 1943 and 22 billion in 1942. The net absorption of 25 billion dollars by the banks followed upon net increases of less than 24 billion in each of the two preceding years. It should be pointed out, however, that the indicated increase in the amount of Government securities taken both by nonbank investors

Treasury Receipts, Expenditures, and Borrowing

(In billions of dollars)

	1941	1942	1943	1944
Receipts and expenditures:				
Income and profits taxes	4.3	11.1	26.6	34.3
Other	4.5	5.3	8.0	10.1
Net receipts*	8.8	16.4	34.6	44.4
War expenditures	13.9	52.4	85.1	91.2
Other†	6.6	5.2	4.7	5.2
Total expenditures	20.5	57.6	89.8	96.4
Net expenditures	11.7	41.2	55.2	52.0
Increase in general fund balance	1.6	7.0	1.8	9.9
Borrowing (increase in interest-bearing debt)	13.4	47.8	57.1	61.6
Net absorption of Government securities:				
Government agencies and trust funds	1.9	2.7	4.7	4.7
Others	7.4	21.6	28.6	31.9
Total nonbank investors	9.3	24.3	33.3	36.6
Commercial banks	4.0	19.6	18.5	17.7
Federal Reserve Banks	0.1	3.9	5.3	7.3
Total banks	4.1	23.5	23.8	25.0

* Exclude net appropriations to Federal old-age and survivors insurance trust fund.

† Includes net expenditures of trust funds and Government agencies except for war and debt retirement.

and by banks in 1944 was swollen appreciably by the inclusion during the year of three War Loan drives—one at the beginning, which had the advantage of accumulations of nonbank funds during November and December 1943, after the close of the Third War Loan; one in the middle of the year; and the final one in November and December, effectively tapping available investment funds right up to the year end. The two War Loan drives of 1943, by way of contrast, enjoyed no carryover of funds from the preceding year (since the First War Loan drive came at the close of 1942) and left a carryover of investment fund accumulations to be invested in the Fourth War Loan in January and February of 1944. Bank holdings of Government securities were increased greatly, despite the absence of large direct offerings to the banks, by heavy purchases of securities from nonbank investors in connection with each of the three War Loan drives.

Government Security Sales And Market Redistribution

During 1944 the Treasury raised the bulk of its borrowed funds through the War Loan drives, direct participation in which was restricted to nonbank investors. Sales of Government securities in the three drives of 1944 reached a total of 59 billion dollars, 16.7 billion in the Fourth drive of January-February, 20.6 billion in the Fifth drive of June-July, and 21.6 billion in the Sixth drive of November-December. In addition, Treasury investment accounts purchased about 1.7 billion dollars of the War Loan issues, and commercial banks were permitted to subscribe to limited amounts (the total came to 2.4 billion dollars) of these securities for the investment of their savings deposits. In neither case, however, were such purchases counted as part of the War Loan drives. The outstanding supply of Treasury bills, for which tenders may be entered by any class of investor without restriction, was increased 3.4 billion dollars during the year. Other funds were raised by the continuous sale of Savings bonds and notes outside the drives, and by net purchases of 3.6 billion dollars of special issues by Government agencies and trust funds. Except in one isolated instance where a maturing obligation was paid off in cash by the Treasury, both nonbank investors and banks were offered new issues in exchange for holdings of matured or called obligations.

The large volumes of Government securities sold to nonbank investors during the War Loan drives cannot, however, be used as a measure of the actual absorption of Government securities by these investors. The

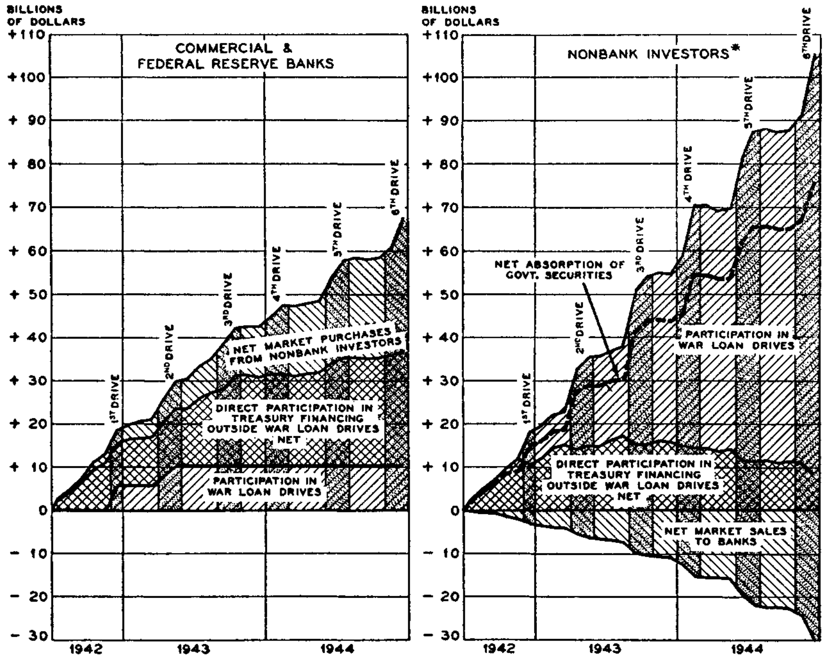
War Loan drive totals never would have reached such magnitudes as 20 billion dollars or more had not nonbank investors greatly augmented their funds available for subscriptions in the drives by selling to the banks securities acquired previously (in many cases in earlier War Loan drives).

There are also other factors, of lesser quantitative importance, tending to build up War Loan drive sales totals relative to the net absorption in Government securities by nonbank investors. The greater part of the Treasury savings (tax) notes acquired in the War Loan drives, chiefly by corporations, are later redeemed in meeting tax liabilities. War bonds are "cashed" as emergencies arise, or when the holders want cash for other purposes. Moreover, there have been distortions or abuses of the War Loan drive mechanism, such as purchases of War bonds which are promptly redeemed at the end of the sixty-day waiting period, "free-riding"—the purchase of War Loan securities for resale after the close of the drive in order to profit from the premiums generally commanded by the drive securities after subscription books are closed—and the padding of subscriptions, to assist in meeting or exceeding quotas for particular communities, or for other reasons, which involved large amounts of subscriptions which could be paid for only with the aid of bank loans or out of the proceeds of sales of other securities.

The amount by which nonbank investors increased their holdings of Government securities during 1944, 32 billion dollars, came to somewhat more than half of total sales to such investors in the three War Loan drives of the year. The difference was accounted for by net market sales of previously acquired securities to the banks, and by an excess of redemptions of Savings notes (over sales outside the drives) for the purpose of meeting tax liabilities. The net market sales to the banks of securities previously acquired by nonbank investors were a principal source of the increase in the growth of commercial and Federal Reserve Bank holdings of Government securities during the year. A part of the growth in Reserve Bank portfolios, however, reflected an increase in the outstanding supply of Treasury bills. Direct allotments of Government securities other than bills to the banks, less redemptions, amounted to only 2 billion dollars.

Shifts of already outstanding Government securities from nonbank investors to the banks were heavily concentrated in the months of the War Loan drives. As nonbank investors drew down their bank deposits during the War Loan drive periods to pay for the new securities, bank reserve requirements were reduced because the deposits were transferred

Absorption of U. S. Government Securities by Bank and Nonbank Investors (Cumulated from June 30, 1942)



* Excluding U. S. Government agencies and trust funds.

to Government War Loan deposit accounts which are exempt from legal reserve requirements; thus the banks were in a position to add substantially to their security portfolios in the drive periods. On their part, nonbank investors were disposed to sell previously acquired securities in order to take profits and to increase their participations in the drives. Thus holdings of Government securities by the banks, as well as those by nonbank investors, showed their principal increases during War Loan drive periods. Between drives total holdings by both nonbank investors and banks tended to show little net change, although there were substantial sales by commercial banks and purchases by the Reserve Banks at such times to enable the former to meet their rising needs for reserves.

Rather definite patterns were evident in the shifts, particularly of Treasury bills and certificates of indebtedness, between the commercial banks and the Federal Reserve Banks. As their reserve requirements dropped during the War Loan drives, the commercial banks not only acquired large blocks of securities through market purchases, but also built up their Treasury bill holdings, either by reacquiring bills previously sold to the Federal Reserve Banks under repurchase option, or by entering tenders for new weekly bill offerings in excess of their current maturities. Between drives, on the other hand, member bank needs for reserves increased as Treasury expenditures converted reserve-exempt War Loan account deposits into private deposits and as the banks drew upon their reserve balances to meet public demands for currency. The member banks covered their needs for additional reserves during such periods by selling Treasury bills directly, and certificates of indebtedness indirectly (through the market) to the Reserve Banks, and at times by borrowing.

Certificates played a much larger role in day-to-day adjustments of bank reserve positions than had been the case in 1943, both through outright purchases and sales and through use as collateral for advances from the Federal Reserve Banks. The banks were generally net sellers of certificates between War Loan drives but they picked up large amounts during the drives, and it is estimated that the commercial banks as a whole added approximately 2.5 billion dollars net to their certificate portfolios during the year.

During 1942 and 1943 banks in fully invested positions generally had sought to maintain Treasury bill holdings at such levels that there would be little risk that their supply would fail to cover needs for short-run adjustments of reserve positions. With the rapid growth in certificate portfolios, the banks permitted their Treasury bill holdings to decline and at the same time became less reluctant to borrow. Additions to Treasury bill holdings during War Loan drives were more than offset by net sales during the interdrive periods. Thus all of the 3.4 billion dollar increase in the outstanding supply of Treasury bills went into the Federal Reserve Bank portfolios and in addition 1 billion previously held by the commercial banks and nonbank investors.

The contracting tendency in the market for Treasury bills represented an extension of a trend that became apparent in the second half of 1943. On June 16, 1943, holdings of Treasury bills outside the Federal Reserve Banks reached a record peak of nearly 9 billion dollars; the corresponding figure for December 27, 1944 was 4.9 billion dollars. The diminution of market demand for Treasury bills is apparently attributable to the relatively unattractive yields afforded and to the availability of ample supplies of certificates and other types of Government securities offering higher rates of return, which the banks could acquire through market purchases from nonbank investors. While the banks were generally compelled to pay premiums above par for such securities under the prevailing method of sale and structure of interest rates, they benefited from the tendency of all such securities to advance in price as their term to maturity became shorter, so that if the securities were resold the actual yields obtainable were even higher than the nominal coupon rates.

Considering the temptations to lengthen portfolios in order to realize the larger returns available upon longer term Government securities, it is gratifying to observe that, on the whole, the commercial banks have continued to maintain substantial proportions of shorter term securities, and so are well fortified to meet the losses of deposits which individual banks may experience during the period of postwar readjustments. The banks which are fully invested and without surplus reserves, primarily the larger institutions, have tended to concentrate well over half of their Government security holdings in notes, certificates, bills, and other securities maturing within five years. Banks not in a fully invested position, principally smaller institutions, are apt to have smaller proportions of Government securities maturing within five years—about 40 to 50 per cent of their total Government portfolios—but these banks have excess reserves and often large balances with city correspondents as an additional resource with which to meet any deposit losses that may occur. When cash assets and short term Government security holdings are taken together and are related to deposit liabilities, the highest proportions are found among the banks which over the war period have experienced the largest deposit increases; it is such banks, in war boom centers, that may be most vulnerable to deposit shifts after the war. On the other hand, deposit gains may be experienced in centers of consumers' goods production and diversified civilian output.

Changes in commercial bank deposits after the war are most likely to take the form of shifts between banks rather than a contraction in the over-all level. In fact, it is likely that there will be strong forces operating to sustain and enlarge the total volume of commerical bank deposits, at least in the early postwar period. War bond sales to individuals will probably fall off and redemptions may accelerate, and a persistence of Federal budgetary deficits, as an aftermath of the war, may be accompanied by a further flow of Government securities to the banks; also business firms may convert some of their Government security holdings into deposits and employ bank credit to some extent in financing reconversion, deferred maintenance, and other capital outlays. A contraction in outstanding currency circulation, and a growth of export financing would also tend to increase total deposits.

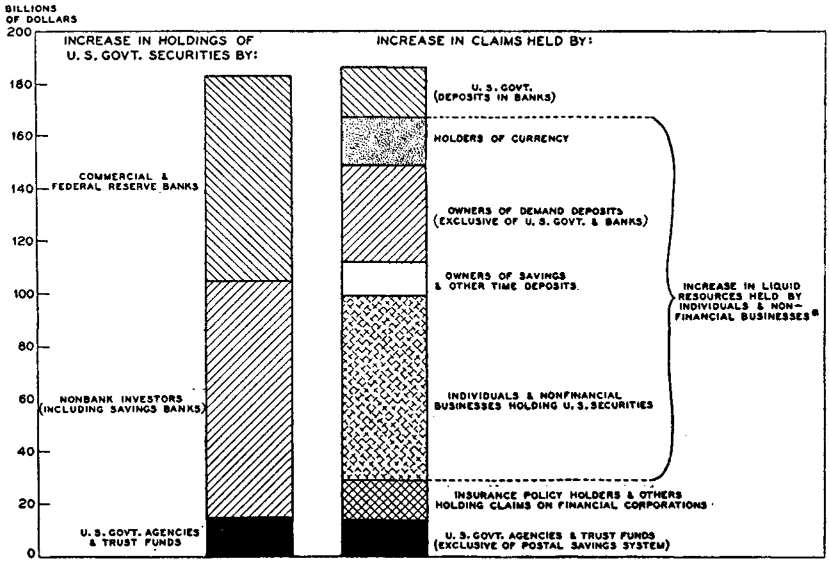
The Debt and the Claims upon It

The great wartime increase in the public debt has had far-reaching effects upon the American economy and inevitably will have a vital bearing upon postwar economic developments and problems. Every dollar of Federal Government debt represents a dollar of assets to some person or organization. It is important to note, however, that the ultimate claims against the debt do not necessarily take the form of Government security holdings. For example, the Federal Reserve Banks provide currency to meet public demands and themselves acquire and hold Government securities which otherwise might have been taken by the public, pledging the securities as collateral for the currency they issue. Similarly, the commercial banks provide checking accounts and time deposits; the savings banks and Postal Savings System provide savings deposits; the insurance companies provide protection against some of the hazards of life—all acquiring and holding (in wartime) mainly Government securities against their increased liabilities. Thus the public either owns directly, or holds indirect claims on practically all the war-increased public debt, including that held by banks and other financial institutions. Under the highly developed financial organization that exists, the public has the option of deciding what sorts of claims it will hold. Within broad limits these claims may also be changed from one kind to another. Thus Government securities held by individuals or business firms may be sold and converted into cash or bank deposits, or vice versa.

The accompanying chart shows, on the left, the actual holders of the Federal interest-bearing debt incurred during the five war years—over and above the 47 billion dollars of debt outstanding at the end of 1939—and, on the right, the accumulation of claims or assets that is the counterpart of the wartime debt accumulation.* Of the 183 billion dollar increase in the public debt, there has been a 15 billion increase in Government securities held by Government agencies and trust funds, an increase of approximately 90 billion in holdings by nonbank investors (including individuals, trust funds, insurance companies, savings banks, other corporations, etc.), and an increase of about 78 billion in holdings by commercial and Federal Reserve Banks.

* The two columns are not of precisely the same height, since some of the collateral for the additional currency supplied during the war years consists of gold certificates, rather than Government securities, and since there have been other factors, such as changes in the volume of bank loans, that have affected the growth in bank deposits. On the whole, however, such factors have been of minor importance; the major factor, both in the growth in the public debt, shown in the lefthand column in the chart, and in the growth in assets or claims held by the public, shown in the righthand column, has been the financing of the war.

Wartime Debt Expansion and the Claims Upon It
(December 31, 1939 to December 31, 1944)



* Includes relatively small holdings of demand and time deposits and U. S. Government securities by State and local governments.

The major claims against the first group are those held by individuals who are entitled to future old-age retirement and unemployment benefits. Government securities held by insurance companies and other financial corporations of various classes other than banks have increased 15 billion, the bulk of which represents reserves against insurance policies and annuities held by the public. These two components, at the bottom of the column, are of a broadly social security character; they are not generally availed of except when the contingency for which they are created occurs.

Of the increase in claims which has been the counterpart of the rapid growth of the Federal debt, by far the largest part is the 137 billion dollars of "liquid asset" accumulation by individuals and nonfinancial businesses. These items are bracketed together on the chart. United States Government deposits, at the very top of the column, represent unspent proceeds from the sale of Government securities. As these deposits are disbursed, the claims are transferred to others — to the recipients of Government checks who in the first instance either deposit them in their bank acounts or cash them, and thus add to the liquid assets of individuals and businesses.

The greatest attention deserves to be focussed upon the long middle section of the right hand column, the four items of ''liquid asset'' accumulation. All of them represent resources which are now spendable—to the extent that they are in the form of currency and demand deposits—or which can be converted into spendable currency or demand deposits more or less readily.

During the war the spending of liquid funds has been held in check, partly by production controls which have made unavailable many things which consumers would otherwise have bought, and partly by the rationing of goods which are still available but not in sufficient amount to meet all demands in a period of high national income. Nevertheless, there have recently been indications of an increasing tendency on the part of the owners of the accumulating liquid assets to spend or invest them. Heavy spending on luxury goods such as jewelry during the recent holiday season and a rather general shift to the buying of higher priced merchandise, rising prices and increased turnover of urban and farm real estate, and a strong upward trend in prices of stocks and other corporation securities—all have given evidence of the increasing tendency to employ available funds in one way or another. It should not be overlooked, however, that the funds so spent or invested are subject to the brake of taxation, not only by reason of substantial excises on luxury goods, but also taxes on the income of producers and distributors and taxes on capital gains.

Considerable discussion has revolved around the postwar disposition of individuals and nonfinancial businesses to part with their wartime accumulations of Series E War bonds (25 billion dollars at end of 1944) and other Government securities (45 billion dollars). This 70 billion dollars alone accounts for a little more than half of the over-all accumulation of liquid assets and more than one third of the wartime increase in the Federal debt. It is already more than three times the accumulation of Government securities by individuals and nonfinancial businesses during the First World War and, like the other components of the column (and the total debt), is still rising.

Less diversity of view has been apparent in expectations as to the uses which business firms will make of their Government security holdings than in the expectations as to what individuals will do with theirs. The common view is that industrial and other nonfinancial business enterprises will reduce their Government security holdings during the reconversion period to meet their accrued tax liabilities and to make necessary or advantageous new capital investments as they find it possible, to rebuild their inventories of consumers' goods, and to take care of deferred maintenance. The concentration of business purchases of Government securities in short term obligations, predominantly Treasury Savings notes (redeemable at the option of the holder either in payment of taxes or for cash) and one-year certificates of indebtedness, strongly supports this interpretation. Over the longer run it appears doubtful that most corporations could justify keeping large amounts of stockholders' capital invested in low-yielding Government securities.

As for individuals, some have held that the predominant tendency will be for them to retain their Government securities, but that the existence of these reserves will increase their disposition to spend current incomes and lessen their disposition to add to their savings. Others think that sales or redemptions will be concentrated in periods of adversity and unemployment, when sale or redemption would serve the double purpose of supporting the holder until jobs are more plentiful and of injecting new money into the income stream. At the opposite pole of expectations there are those who believe that sales and redemptions of Government securities will be heaviest when business is prosperous, jobs assured, confidence is running high, and other investment opportunities tempting.

In reality, it is too much to expect that we can foresee with any degree of precision what the patterns of individuals' purchases, sales, and redemptions of Government securities will be over the years to come. A great deal depends upon the competition of other investment opportunities, the kinds of Government securities that are then offered, interest rates, the availability of credit in financing private expenditures, price and income levels, taxation, and debt retirement. For the immediate postwar period it does appear that redemptions of War bonds (and also of Savings notes, held largely by business firms) will be apt to run to considerably larger totals than have heretofore been experienced. Clearly, there are strong pent-up demands resulting from the necessary diversion of manpower, materials, and productive facilities to meet the imperative needs of the war, and it would be natural to expect that some Government securities, along with other liquid resources and credits, will be employed to finance the satisfaction of these demands.

Government securities held by individuals and nonfinancial businesses have been defined as "liquid assets," along with currency and bank deposits, because they are readily convertible into currency or deposits. Nevertheless, a line of distinction may be drawn between Government security holdings (and at least some savings deposits) on the one hand, and checking account deposits and currency holdings, on the other. There are, that is to say, graduations of liquidity and also of likelihood that various types of liquid assets accumulated during war will be spent. The interest income that is lost, together with the fact that Government securities and savings deposits must ordinarily be converted into checking account deposits or currency before being spent, imposes some restraint upon the use of such resources for making expenditures. This is one of the considerations which has led to the emphasis upon the distribution of the maximum possible amount of Government securities to "nonbank" investors in financing the war.

Liquid asset accumulation in the forms of currency held by the public and deposits with the commercial banks has been rapid and continuous. During the past two years currency circulation has been increasing at a rate of about 5 billion dollars a year, and commercial bank demand deposits, exclusive of U. S. Government and interbank deposits, have maintained an annual rate of growth of roughly 9 billion over the same period.

Clearly there has been an increased need both for currency and checking account deposits to meet additional working cash requirements incident to the extraordinary expansion in production and trade over the war period. When we relate the expansion in currency and bank deposits to the expansion in production and trade and the volume of money transactions, however, it becomes equally clear that the growth in the "money supply" has run far ahead of the needs. It is particularly striking that currency circulation and checking account deposits have failed to show a leveling off tendency in consonance with the relative stabilization of war expenditures, gross national product, employment, and prices during the past year.

Just what considerations have motivated the continuous accumulations of currency and deposits has been the subject of much speculation. Among the many explanations that have been offered are high "liquidity preferences" on the part of the public, which may be partly an aftermath of speculative misadventures of the twenties; low interest returns on Government securities and high income taxes which weaken financial incentives for investment; widespread movements of individuals and families from one location to another which tend to enlarge cash require ments; and (in the case of currency) the desire to conceal resources for tax and other purposes and to conceal illicit transactions. Probably most or all of these considerations enter into the true explanation. In any event the uses made of these resources will have vital influences upon postwar levels of income and the purchasing power of the dollar. Together with Government security and savings deposit holdings they can provide a valuable cushion for postwar adjustments in periods of economic adversity. Contrarywise, they can generate demands for goods and services in excess of the nation's capacity to produce and so could set in motion a strong inflationary spiral.

Under such circumstances there are three principal courses which might be pursued in seeking to maintain the economy on a reasonably even keel, to provide employment opportunities for substantially all those seeking work and to oppose tendencies of inflation or deflation of the income and price structures. One course would be to rely extensively upon Government fiscal policy—through controlling the kinds and magnitudes of taxation and expenditure and through management of the public debt. Another would be to influence the cost and availability of credit to business and other borrowers and the interest return offered to investors, so as to influence rates of investment and saving. A third course would be to rely upon direct controls, such as the wartime controls over prices and wages, and the terms upon which credits may be granted. It seems possible that measures of all three types, properly coordinated, may be required in differing degrees to achieve the objective.

It is inevitable that tax, spending, and debt management policies of the Federal Government will be of vital importance in governing the degree of utilization of our economic resources after the war. The magnitudes of revenues and expenditures will be higher than in any other peacetime years. It will be important not only that the right amounts of taxes are collected but that the right kinds of taxes are levied, and so too with expenditures. The war has emphasized the enormous productive capacity of the American economy. When peace comes the strain and tempo will slacken and the long working hours disappear, but the people of this country can still enjoy a higher standard of living than ever before in peace or in war. It will take our best collective judgment, however, to provide the appropriate incentives, and the appropriate distribution of rewards, to make this potentiality an actuality.

Federal Reserve Policy and Operations

Continuing full-scale war operations throughout the year demanded a continuance of Federal Reserve policy directed to the same objectives as in preceding war years. There must be no lack of reserve funds necessary to the financing of the war effort. But the huge scale of war financing operations, and continued limitations on the availability of civilian goods, necessitated constant emphasis on efforts to minimize inflationary pressures by seeking to finance the war as largely as possible outside the banks and to avoid unnecessary expansion of bank credit. Member banks had to be supplied with large amounts of reserve funds to enable them to meet demands on them arising out of the war situation, and from time to time the Federal Reserve System also found it desirable to intervene in the Government security market for the purpose of exerting a stabilizing influence, but within these limits excessive increases in the credit supply were to be avoided.

Member bank needs for reserve funds led to a greater expansion in the volume of Federal Reserve credit outstanding than in any previous year—an increase of approximately 7½ billion dollars. The reasons for the record volume of Federal Reserve credit extended were as follows:

1. The previous exhaustion of excess reserves in most of the large city banks and many others;

2. The absence of special factors tending to reduce the banks' needs for reserves (such as the removal early in 1943 of reserve requirements against Government War Loan deposits for the duration of the war);

3. The heavy demand for reserve funds arising out of continued large demands for currency, the conversion into gold of dollar balances acquired by foreign central banks and governments, and a continued increase in member bank reserve requirements accompanying further growth in deposits.

The various factors affecting the demand for Federal Reserve credit during 1944 and the actual amount supplied are summarized in the accompanying table, in which corresponding figures for the three preceding war years are given for comparative purposes.

It will be observed that, despite the tapering off in the rate of the wartime increase in industrial payrolls and in the national income, the

Factors Affecting the Reserve Position of Member Banks and the Need for Federal Reserve Credit

	(In millions of dollars)			
	1941	1942	1943	1944
Factors affecting member bank reserves:				
Increase in currency circulation	— 2,428	— 4,250	— 5,039	— 4,858
Net Government expenditures (+) or receipts (—)	— 341	+ 1,211	— 164	+ 104
Gold and foreign account operations, net	+ 1,101	— 30	— 1,355	— 1,163
All other	— 15	— 573	+ 761	— 159
Total	— 1,683	— 3,642	— 5,797	— 6,076
Increase in required reserves	+ 1,927	+ 1,771	+ 499	+ 1,112
Net increase in need for reserves	+ 3,610	+ 5,413	+ 6,296	+ 7,188
Change in excess reserves	— 3,523	— 1,095	— 736	+ 314
Federal Reserve credit in use	+ 87	+ 4,318	+ 5,560	+ 7,502

net increase in the amount of currency outstanding was nearly as great in 1944 as in 1943. In fact, had it not been for the use of fairly sizable amounts of previously accumulated currency to pay for war bonds during the Sixth War Loan, the increase during the past year might have been fully as great. The loss of reserve funds involved in net payments to foreign countries for raw materials, supplies, and services furnished to our armed forces abroad, etc., continued during the first half of the year at a rate fully as rapid as in 1943, but subsequently proceeded less rapidly, and for the year as a whole was somewhat less. The third major factor affecting the reserve position of member banks was a substantial rise in their reserve requirements, which accompanied the continued increase in their deposits. In this case the 1944 increase was nearly double that of the previous year, chiefly because the 1943 increase was substantially reduced by the removal, early in the year, of the reserve requirement against War Loan deposits. But compared with 1941 and 1942, the 1944 growth in the required reserves of member banks remained relatively small.

The means of supplying needed reserves to member banks showed further changes during 1944 in the directions indicated in the previous year. The gradual weakening of member banks' disinclination to borrow from the Reserve Banks to obtain needed reserve funds which was observed in 1943, continued during the past year, although this tendency was reflected only to a minor extent in member bank and Federal Reserve year-end statements. The number of member banks in this District which borrowed from the Reserve Bank at some time during the year increased further to 202 compared with 148 in 1943. Included in that figure were a number of the largest New York City banks, as well as many smaller banks throughout the District. In general, member bank borrowing tended to build up in the periods between War Loan drives, reaching its maximum shortly before the issue date for drive securities, and then to drop sharply during War Loan drives when substantial amounts of reserves were released by the shift of deposits from private accounts into War Loan accounts. The number of borrowing banks reached its maximum for any month in recent years in May, when 116 banks in this District borrowed at some time during the month. The greatest aggregate amount of borrowings for any month, however, was reached in November, when 100 banks in the District obtained loans from this bank aggregating about 2,850 million dollars. Some of these loans, however, were for only very short periods, and the maximum amount of loans to member banks on the books of this bank on any weekly statement date was 464 million dollars on November 29. That was the highest figure in more than eleven years. While something of the same trend was evident in other parts of the country, the amount of Federal Reserve credit so extended in other areas was relatively small compared with the total volume of reserve funds needed by member banks.

The major source of additional reserve funds for member banks in the country as a whole, and for banks in this District as well, continued to be purchases of United States Government securities by the Reserve Banks. Here again, trends observed in 1943 continued in 1944—as was pointed out in a preceding section of this report, member banks held fewer Treasury bills and substantially more Treasury certificates of indebtedness, and consequently obtained less of the reserve funds they needed through sales of bills to the Reserve Banks and more through sales of certificates in the market (many of which were purchased in the market by the System Open Market Account). A considerable part of the Treasury bills bought by the System were acquired indirectly from additional issues by the Treasury. The volume of certificates of indebtedness acquired by the System is obscured in the accompanying table owing to the fact that on more than one occasion during the past year a maturing issue of certificates was refunded with an issue of short term Treasury notes. The figures for certificates and notes, consequently, may appropriately be considered together.

Changes in Government Security Holdings of All Federal Reserve Banks

	(In millions of dollars)		
	1942	1943	1944
Treasury bills	+ 1,000	+ 5,758	+ 4,380
Certificates of indebtedness	+ 1,041	+ 1,426	+ 2,419
Treasury notes	+ 547	− 659	+ 901
Treasury bonds	+ 1,315	− 1,217	− 316
Government guaranteed issues	+ 32	+ 46	− 81
Total	+ 3,935	+ 5,354	+ 7,303

Reserve Bank purchases of Treasury certificates in the market were not limited to those sold by member banks, although other purchases served the dual purpose of stabilizing the market and at the same time providing the banks with reserve funds. Insurance companies and other corporations that had bought certificates as temporary investments, sold substantial amounts in the market before War Loan drives to obtain funds for investment in the new issues, and in addition some corporations sold certificates before tax dates to raise funds with which to meet their tax payments. While others, such as Government security dealers and banks with surplus funds, absorbed some of the supply, the Federal Open Market Account usually found it necessary at such times to purchase substantial amounts of certificates in order to maintain reasonably stable market conditions. Ultimately, of course, the volume of System purchases of Government securities was determined primarily by the banks' needs for reserves.

While the Reserve Banks saw to it that the banks were provided with the volume of reserve funds they needed, at the same time they found it necessary in each War Loan drive to adopt measures designed to restrain excessive expansion in bank holdings of Government securities. The pressure to reach sales quotas during the drives and the usual rise in market prices of Government securities following each drive created a situation in which patriotism and profit became intermingled. On the one hand, subscriptions by nonbank investors were entered for much larger amounts of Government securities than they were able to pay for out of their own available funds, the remainder being financed with bank loans, which were subsequently liquidated with the proceeds of securities sold at a profit—mostly to banks—in the period following each War Loan. Alternatively, securities previously purchased by nonbank investors were sold—at a profit and mostly to banks—in order to provide funds for "padded" subscriptions in succeeding drives. This process was stimulated by the fact that no direct offerings to the banks of Government securities (other than Treasury bills) were made during 1944.

As a corollary, a definite abuse of the War Loan deposit account mechanism appeared to be developing through the overeagerness of banks to acquire, and nonbank investors to sell, Government securities especially prior to, during, and immediately following Loan drives. Banks were soliciting sales of outstanding securities, either directly from customers and others or through the Government securities market, with the understanding that the sellers would use the proceeds of such sales to pay for subscriptions entered through these banks for substantially equivalent amounts of new securities offered during the drives. In other cases the initiative appeared to have come from security holders, who wished to sell the securities to a bank (perhaps at a price above the prevailing market), with the same understanding with respect to a subsequent subscription to be made through the bank. In either case the banks appeared to be encouraging sales of Government securities which the banks could purchase with deposits that would be converted into War Loan deposit balances when the sellers subscribed for new securities during the drive, an undesirable practice in itself, and one which exaggerated natural adjustments in security portfolios.

The Reserve Banks cooperated with the Treasury in the effort to discourage such practices and to minimize speculative subscriptions. In a circular letter, dated November 13, 1944, which was sent to all banking institutions in the Second Federal Reserve District, the President of this bank called attention to the practices which were considered abuses of the War Loan procedure, or otherwise undesirable, and requested the banks' cooperation in avoiding and discouraging them.* Similar letters were sent by the Presidents of other Reserve Banks to commercial banks in their districts. The circulars containing detailed information concerning War Loan drives regularly included requests that speculative subscriptions be discouraged.

The amount of bank credit expansion involved in the Fourth War Loan (January-February 1944), in the form either of bank loans or of bank purchases of outstanding Government securities to provide funds for the financing of subscriptions by nonbank investors, was considerably

* Circular No. 2865.

less than in the Third War Loan (September-October 1943). In the Fifth War Loan, however, the amount of bank credit involved was again very large. In the Sixth, the volume of loans was somewhat less, but the increase in bank holdings of securities (exclusive of Treasury bills) was fully as large as in the Fifth Loan. As a result, various possible measures to reduce the "padding" of War Loan totals with bank-financed subscriptions were under consideration at the year end.

Reserve Ratio of Federal Reserve Banks

The factors responsible for the heavy demand for Federal Reserve credit during the past year were also responsible for a further decline in the combined reserve ratio of the twelve Federal Reserve Banks. From a peak of about 91 per cent at the end of 1941 (which resulted from the heavy inflow of gold during the early war years and prewar years), the ratio of reserves to deposit and note liabilities of the Reserve Banks declined at the end of 1944 to slightly under 50 per cent.*

The major cause of the decline in the reserve ratio of the Federal Reserve Banks was the persistent public demand for currency, which increased the amount of Federal Reserve notes in circulation from about 8.1 billion dollars at the end of 1941, to 21.5 billion at the end of 1944. Second in importance has been the loss, through settlements with other countries, of a part of the gold that came to the United States during the early years of the war. Total reserves of all twelve Reserve Banks were approximately 2.2 billion dollars less at the end of 1944 than at the end of 1942, although they were still more than 3 billion greater than at the end of 1939. Third in importance has been the increase in deposits of Federal Reserve Banks, which has reflected mainly the growth in member bank reserve requirements arising out of the rapid growth in bank deposits since this country entered the war. The increase in member bank reserve deposits in the Federal Reserve Banks amounted to slightly more than 1 billion dollars between the end of 1941 and the end of 1944; it would have been much greater but for the fact that member banks entered this period with a large amount of excess reserves. Deposits of foreign central banks and governments in the Reserve Banks also increased during the three year period, despite the conversion of a large

* The reserve ratio of this bank or any other individual Federal Reserve Bank is of less significance than the average ratio for all twelve Reserve Banks, as it is affected not only by those factors which affect the position of the Reserve Banks as a whole, but also by interdistrict movements of funds and the reallocation, from time to time, of Government security holdings of the Reserve Banks.

part of the dollars acquired by foreign countries into gold, but the increase in such deposits was offset by net reductions in other deposits, including the Treasury's working balance in the Reserve Banks.

The rapid reduction in the reserve ratio of the Federal Reserve Banks, during the year, necessitated consideration of the steps to be taken if the ratio continued to decline during 1945, and approached the minimum required reserve percentages specified in the Federal Reserve Act. A review of the situation revealed a number of alternative courses of action by which the reserves of the Federal Reserve Banks could be increased to some extent, or the growth in the deposit and note liabilities retarded. Most of these measures, however, would give only limited or temporary relief, and it became clear that if the downward trend in the reserve ratio should continue for an extended period, more direct, candid, and far-reaching adjustment would be desirable. There was general agreement that it would be unthinkable that the Federal Reserve Banks should fail to give the necessary support to the war financing program because of a technical reserve requirement, established at the beginning of the System in 1914, and the main question, therefore, was what method of dealing with the situation would provide the best solution.

The problem is by no means peculiar to this country; in fact, it arose much later in the United States than in most other countries that are active participants in the war, chiefly because of the huge inflow of gold during the six years before the war and in the two years after it started, which resulted in the concentration in this country of about three fifths of the world's known monetary gold stock. Most of the other active belligerents, if they had not already modified or abandoned the former reserve requirements of their central banks before the outbreak of the war, did so during the early years of the war.*

After full consideration of the various alternatives, it was concluded that the best solution would be to seek reduction, by the Congress, of the legal reserve requirements of the Federal Reserve Banks, retaining requirements that would compare favorably with those of most other countries, meet the views of the public with respect to their adequacy, and yet provide sufficient further leeway for the Reserve Banks. There must be no question of the ability of the Federal Reserve System to provide a sound currency in the amounts required by the public, and

* See "Wartime Changes in Foreign Central Bank Reserve Requirements" in the September 1944 issue of the *Monthly Review of Credit and Business Conditions* of this bank.

at the same time to keep the commercial banking system adequately supplied with reserves so that it can continue to do its part in the war financing program. Specifically, it was proposed that in place of the present minimum reserve of 40 per cent in gold certificates against Federal Reserve notes and 35 per cent in gold certificates *or* "lawful money" against deposits, a uniform minimum reserve of 25 per cent, exclusively in gold certificates, be required against Federal Reserve notes and deposits alike. (On February 12, 1945 legislation to effect this change was introduced in Congress). The former distinction between reserves against notes and deposits was considered meaningless in view of the fact of the ready convertibility of notes into deposits and deposits into notes.

Business and Financial Developments in the Second Federal Reserve District

There have been indications during the past year that business activity in this District, as in the country as a whole, was approaching or had passed its wartime peak. Whereas in previous war years this District had lagged appreciably behind the rest of the country in the rate of expansion, in 1944 various indicators showed no great difference between the District and the country as a whole.

	Percentage changes from the preceding year				
	1940	1941	1942	1943	1944
Income payments to individuals					
United States*	+ 7.4	+ 21.6	+ 24.4	+ 20.3	+ 8.5 *e*
Second F. R. District *e*	+ 5.6	+ 14.2	+ 14.7	+ 15.6	+ 7.6
Department store sales					
United States	+ 6.8	+ 17.0	+ 12.6	+ 12.3	+ 10.9
Second F. R. District	+ 4.7	+ 12.7	+ 7.0	+ 5.8	+ 10.4
Factory employment					
United States	+ 7.5	+ 22.9	+ 16.6	+ 14.1	− 5.2
New York State	+ 7.8	+ 19.8	+ 10.8	+ 9.1	− 6.5
Factory payrolls					
United States	+ 14.5	+ 46.3	+ 46.4	+ 34.7	+ 1.2
New York State	+ 13.0	+ 40.3	+ 34.0	+ 26.8	− 0.2

* Excluding offshore payments to military and civilian personnel.
e Estimated by Federal Reserve Bank of New York.

Sources: Income payments — United States Department of Commerce; department store sales — Board of Governors and Federal Reserve Bank of New York; factory employment and payrolls — United States and New York State Labor Departments.

As these data indicate, total income payments to individuals continued to increase in 1944, but at a slower rate than in the three previous years. In this District the increase appears to have been nearly as large as in the country as a whole for the first time during the war period. For the whole war period (1939-44), the District has shown an increase of approximately 72 per cent, compared with an increase of about 112 per cent for the United States.

Similarly, department store trade in this District increased less than 50 per cent between 1939 and 1944, whereas in the entire country there was an increase of 75 per cent. The increase in this District in 1944, however, was the largest since 1941 and was nearly equal to that for the whole country for the first time during the war period. (The country-wide figure for 1944 showed the smallest gain in sales since 1940, probably owing mainly to limited supplies of merchandise of various types.)

The number of factory workers employed during 1944 was smaller than in 1943 in all of the principal industrial centers of the District. With a few exceptions, the largest reductions occurred in localities where the preceding expansion had been greatest, such as Buffalo and the Albany-Schenectady-Troy area in New York State, and Bridgeport, Connecticut. There were also substantial reductions in factory employment in some cities of the District which had shown less expansion previously, although there were exceptions such as the Paterson, New Jersey, area, which had previously been among the communities showing the greatest expansion, and which had a relatively small shrinkage in employment during the past year. For New York State as a whole, the decline during the past year was about 6½ per cent — a little more than for the country as a whole, but the disparity was much less than in most of the previous war years. Factory payroll disbursements in New York State were only fractionally less in 1944 than in 1943, and in the entire country were only slightly greater, but here again the disparity between New York State and the entire country was much less than in other recent years.

Banking Developments

Banks in this District, especially the New York City banks, continued to be subject to heavy drains on their reserves (through currency demands and losses of funds to other districts and to foreign countries) during the past year, so that large extensions of Federal Reserve credit were necessary to maintain their reserves at the required levels. As the accompanying table indicates, the aggregate loss of reserve funds for all member banks in the District amounted to 4.4 billion dollars in 1944, only slightly less than in 1943, and more than in any previous year. Since the excess reserves of banks in this District had been largely exhausted early in the war period, and since their required reserves continued to rise, the amount of Federal Reserve credit needed was substantially greater than in any previous year.

Gains and Losses of Member Bank Reserve Funds in Second Federal Reserve District

	In millions of dollars			
	1941	1942	1943	1944
Gain or loss through:				
Net Treasury transactions	− 490	− 2,260	− 4,428	− 1,942
Net commercial and financial transactions	− 1,745	− 1,929	+ 1,080	− 935
Increase in currency in circulation	− 505	− 679	− 1,002	− 986
Gold movements and other foreign transactions	+ 761	+ 650	− 212	− 516
Change in nonmember and other deposits in Federal Reserve Bank	+ 1	+ 153	+ 50	− 41
Total	− 1,978	− 4,065	− 4,512	− 4,420
Federal Reserve credit	+ 60	+ 3,455	+ 3,746	+ 4,711

The greatest changes among the factors affecting the reserves of banks in this District in 1944, compared with the previous year, were a substantial reduction in the loss of funds through Treasury transactions, a loss instead of a gain through commercial and financial transactions, and a larger loss through foreign transactions. During the war years payments to the Treasury by banks in this District for their customers and for their own account have been consistently and substantially greater than payments by the Treasury arising from Government disbursements. The net loss during the past year, however, was less than half as great as that of 1943. Federal tax collections in this District continued to increase and represented about the same percentage of collections for the entire country as in previous years, but there was an approximately equal increase in Government expenditures in this District (at least in the volume of Government checks deposited in banks in the District). The reduced drain on the reserves of Second District banks from this source consequently is to be found mainly in somewhat smaller Treasury receipts from borrowing operations. On the whole, some further progress was made in the direction of selling Treasury securities in other parts of the country more nearly in proportion to Government expenditures in those areas, so that the Second District accounted for a slightly smaller proportion of the funds raised in War Loan drives in 1944 than in 1943. The actual amount of funds raised by the Treasury in this District through War Loan drives increased further, however, and the net reduction in the amount of funds raised by the Treasury in the District is accounted for by considerably reduced net sales of Treasury bills, a large part of which are sold in this District, including bills purchased indirectly for the account of this bank and other Federal Reserve Banks.

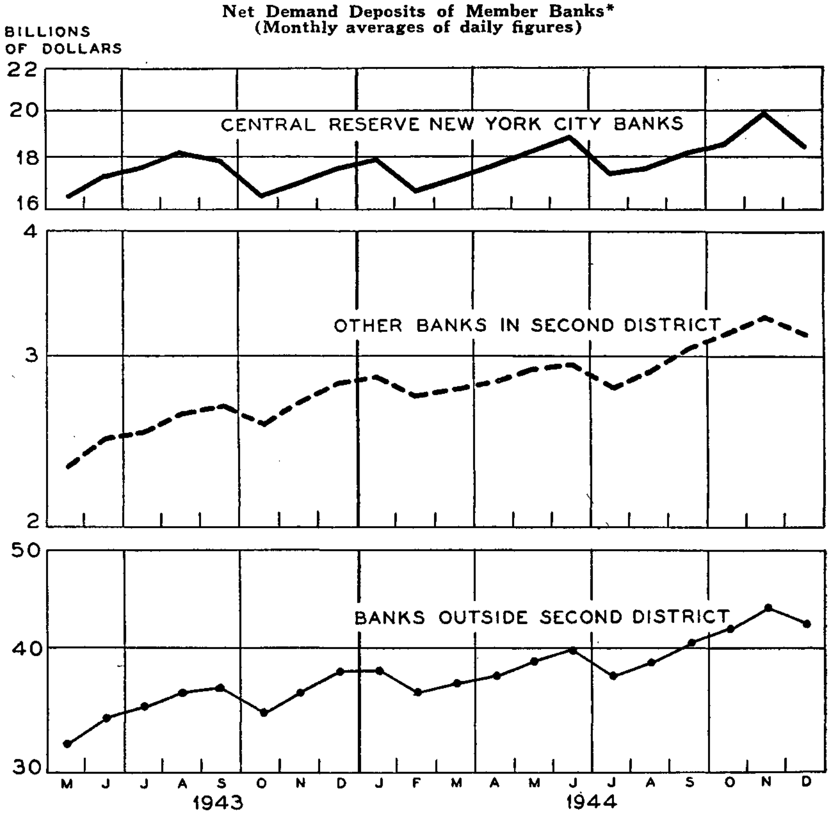
The net loss of funds through commercial and financial transactions, following a net gain in 1943, is largely, though not entirely, explained by the occurrence of three War Loan drives during the past year, compared with two in 1943. There is regularly a substantial outflow of funds from New York City during War Loan drives, followed by some inflow subsequently which reflects the redistribution of War Loan securities through the New York market. As the Sixth War Loan came close to the end of 1944, the year included the usual outflow of funds during the drive, but not the ensuing return flow which was carried over to the early weeks of 1945.

Demands for currency through banks in this District continued heavy during the past year, and net payments of currency by the Federal Reserve Bank of New York again totaled close to 1 billion dollars. On three or four occasions during the year — chiefly during War Loan drives and income tax periods — the outflow of currency was retarded or even reversed, but in the intervening periods the outflow was about as rapid as ever.

Foreign account transactions resulted in a greater loss of funds to banks in this area in 1944 than in 1943, in marked contrast to the earlier war years when they resulted in net gains of funds to banks in the District. These losses took the form of transfers of funds from commercial banks to accounts of foreign central banks and governments on the books of the Federal Reserve Bank of New York, a large part of which was converted into gold and placed under earmark, and in some cases subsequently exported.

The growth in total deposits of member banks in this District during 1944, including Government deposits which were at a very high level at the year end, was as great as in any preceding war year. The net growth in private deposits was comparatively small. This small increase during the calendar year gives a somewhat misleading impression, however, owing to the timing of War Loan drives which regularly absorb substantial amounts of private deposits; deposits were relatively low in December because of the Sixth War Loan, whereas they were relatively high at the beginning of the year because of the accumulation of deposits just prior to the Fourth War Loan. The fluctuations in deposits caused by War Loans are illustrated by the accompanying chart, which shows monthly data on net demand deposits in member banks in New York City, other Second District banks, and member banks in all other Federal Reserve Districts. As this chart indicates, the net growth in the demand deposits of central reserve New York City banks has been considerably slower than in other member banks, either in the remainder of the District, or in the other eleven Federal Reserve Districts. The

Net Demand Deposits of Member Banks*
(Monthly averages of daily figures)



*Plotted on ratio scale to show proportionate changes.

growth of deposits between War Loan drives is fully as great in New York City banks as in other banks, but a larger proportion of the growth between drives is absorbed by subscriptions to War Loan securities during the drives. Member banks in the Second District, exclusive of New York City, have shown much the same trend and fluctuations in their deposits as have member banks in the other eleven Federal Reserve Districts. In each case, however, it appears that despite the huge volume of subscriptions for Sixth War Loan securities, that Loan absorbed a smaller proportion of the preceding deposit growth than any of the four preceding War Loans. This is equally true for banks in this District and for banks in other districts.

The principal change in assets of member banks in the Second District was, of course, a further substantial increase in holdings of Government securities. The net increase in such holdings was 3.9 billion dollars, a somewhat larger increase than in 1943, but less than two-thirds the increase in 1942. The greater increase in Government security holdings during the past year than in the preceding year is explained by the heavy sales of securities to the banks in connection with War Loan drives, of which there were three in 1944 and two in 1943. Loans on securities — chiefly Government securities — showed a greater net increase during the past year than in the preceding year because the Sixth War Loan came so close to the end of the year. Changes in holdings of different types of Government securities during each of the past five years are shown in the following table.

While there was some evidence during the year of a tendency for banks to purchase somewhat longer term securities than in the two preceding years, the trend does not appear to have been particularly striking in this District. It will be noted that net increases in holdings of

Holdings of Government Securities by All Member Banks in the Second Federal Reserve District

Year	Net change in holdings during year, in millions of dollars					
	Treasury bills	Certificates of indebtedness	Treasury notes	Bonds	Guaranteed obligations	Total
1940	— 101	—	+ 465	+ 603	+ 332	+ 1,299
1941	+ 110	—	+ 408	+ 905	+ 127	+ 1,550
1942	+ 1,636	+ 2,413	+ 586	+ 2,362	— 726	+ 6,271
1943	— 485	+ 1,563	— 71	+ 2,327	— 137	+ 3,197
1944	— 456	+ 430	+ 2,314	+ 2,475	— 830	+ 3,933

Treasury bonds in 1944 were not much greater than in the two preceding years. The most striking change has been the substantial reduction in holdings of Treasury bills during the past two years, following a large increase in 1942. The resumption of the use by the Treasury of certificates of indebtedness in that year provided an investment instrument which has proved to be considerably more attractive to the banks than the Treasury bill, so that in subsequent years the banks in this District have increased their holdings of certificates (and notes) even though they found it necessary to dispose of Treasury bills in order to adjust their reserve positions. Much of the increase in holdings of Treasury notes in 1944 should be regarded as the equivalent of an additional increase in certificates of indebtedness, in view of the fact that on two occasions Treasury notes of short maturity were issued in exchange for maturing certificates.

Largely as a result of the continued increase in holdings of Government securities, bank earnings continued to grow, and for the year 1944, net profits were the highest since the late twenties.* Gross earnings of member banks in this District remained substantially lower than in the late twenties (35 per cent below the 1929 peak), and although there has been a considerable reduction in some expenses—chiefly in interest payments on deposits — other expenses including taxes have increased, and net earnings also were more than one-third below the predepression peak. In 1944, however, the banks had substantial profits on sales of securities and recoveries on assets previously charged off, compared with a moderate amount of net charge-offs in 1929, so that their net profits, after these adjustments, were only about 10 per cent less than the 1929 record. In all such comparisons, it must be remembered that membership in the Federal Reserve System in this District now includes a larger proportion of all banks than in the twenties; however, the comparisons are probably not seriously distorted by this factor.

Income taxes are becoming a factor of some importance to the banks, although many still had charges against their income sufficient to exempt them from tax payments in 1944, and only a few banks had reached the point where they were subject to excess profits tax payments. It is expected, however, that the number of banks subject to income and excess profits tax will increase considerably during the coming year, so that tax payments will exert a restraining influence on further growth in bank profits.

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* *See* Circular No. 2911 of the Federal Reserve Bank of New York.

International Monetary and Financial Reconstruction

In this bank's report for 1943 was presented a brief summary of plans which had been developed by experts of the American and British Treasuries for international monetary and financial reconstruction. The American monetary plan (commonly referred to as the White plan) was for a 5 billion dollar International Stabilization Fund, to consist of gold and national currencies contributed by participating countries, each such country being entitled to obtain from the Fund, within certain limits, the currency of any other member in exchange for its own. The British monetary plan (or Keynes plan) was for an International Clearing Union which, though requiring no advance contributions, would have permitted "overdrafts" by member nations in dollars and other currencies up to an aggregate amount in excess of 30 billion dollars. Neither the American nor the British Government committed itself to either of these plans, which were put forward merely as a basis of discussion. Some months later the United States Treasury published a draft proposal for a 10 billion dollar Bank for Reconstruction and Development of the United and Associated Nations for the purpose of making and guaranteeing reconstruction loans to war-stricken countries and long term development loans to these and other countries.

During 1943 and the early months of 1944 these three proposals were the subject of active discussion in financial and economic circles and in the press. There was widespread agreement, in the United States and in other countries, on the general aim of providing a basis for international financial cooperation after the war, as a means of promoting currency stability, restoring international trade, and raising world living standards. Many students of the problem, however, found serious fault with the particular methods proposed in the two currency stabilization plans, and a number of alternative plans were advanced.

In April 1944, following several weeks of discussion between the American and British Treasury experts and monetary experts of other United Nations, a Joint Statement by Experts on the Establishment of an International Monetary Fund was released in Washington and London. The International Monetary Fund which it proposed was to be made up of national contributions in gold and local currencies after the manner of the White plan, but the new plan contained certain changes which brought it more nearly in line with the viewpoint of the British experts and that of various critics of the previous plans. The principal changes were: an increase in the Fund's size to 8 billion dollars; a change giving the economically most important countries slightly greater weight in the administration of the Fund; a recognition of the special problems and special needs of the transition period following the war, in the form especially of (a) the exclusion of relief and reconstruction financing from the Fund's scope, and (b) permission for member countries to continue exchange control as long as may be necessary during the postwar transition period; provision for greater exchange rate flexibility; and a provision that, if the Fund should run short of any currency, other member countries may impose limitations on the freedom of exchange operations in the scarce currency.

In presenting the Joint Statement to the Senate and House committees concerned, the Secretary of the Treasury stated that it represented an agreement on principles by the technicians of some of the 30 United Nations. He pointed out that no government was bound by the statement, but that it was hoped soon to call a formal conference of the United Nations to consider the subject.

On May 26 a United Nations Monetary and Financial Conference was called by President Roosevelt, to begin July 1 at Bretton Woods, New Hampshire, for the purpose of formulating definite proposals for an international monetary fund and possibly also a world reconstruction and development bank. On June 23, in announcing the names of the American delegates, headed by Secretary Morgenthau, the President stated that any agreements reached would not be binding "either morally or legally on the Governments represented, but will be referred to the respective Governments for adoption or rejection." On the other hand, the President instructed the American delegation not to agree to any modifications of the principles of the Joint Statement which were not essential to the effectuation of an agreement, and then only "provided that such modifications do not fundamentally alter the principles set forth in the joint statement." Similarly, the delegates were instructed not to depart from the principles already agreed upon by the American experts with respect to an international reconstruction bank.

The Bretton Woods conference, attended by delegates from all of the United and Associated Nations, convened on July 1 under the chairmanship of Secretary Morgenthau and lasted three weeks, during which it elaborated detailed articles of agreement covering an International Monetary Fund and an International Bank for Reconstruction and Development. Resolutions were also adopted on certain other financial and economic matters, including a resolution calling upon the governments, with a view to creating the economic conditions necessary for the attainment of the Fund's purposes, to reach early agreement on the reduction of international trade obstacles, the orderly marketing of staple commodities, the solution of problems related to the cessation of war production, and the harmonization of national policies for the promotion and maintenance of high employment levels and rising standards of living.

As it emerged from the Bretton Woods conference, the plan for an International Monetary Fund was substantially the same as that contained in the Joint Statement of April 21, but the provisions were much more detailed. The proposed Fund is to have aggregate resources of 8.8 billion dollars instead of 8.0 billion dollars, and of the total, 2,750 million dollars is to be contributed by the United States, 1,300 million dollars by the United Kingdom, 1,200 million dollars by the U. S. S. R., 550 million dollars by China, 450 million dollars by France, and the remainder in specified amounts by the other United and Associated Nations. The amount contributed by each member is called its quota, which is to be paid (with certain exceptions) one fourth in gold and three fourths in the member's local currency Each member is to be entitled to buy foreign currencies from the Fund at par, in exchange for its own currency, up to the amount of its quota plus the amount of gold it will have contributed. Ordinarily, however, a member would not be entitled to get from the Fund more than one fourth of its quota in any one year. Each member is to agree with the Fund on the par value of its currency, and undertakes to cooperate in the promotion of exchange stability, in the avoidance of competitive currency depreciation, and, eventually, in the elimination of exchange controls (except over capital movements) and discriminatory exchange practices. However, when faced by a condition of "fundamental disequilibrium," a member is free to alter the par value of its currency by as much as 10 per cent after merely consulting the Fund, by an additional 10 per cent after giving the Fund three days' notice and provided the Fund raises no objection, and beyond 20 per cent if the Fund does not object within a longer but unspecified period. The Fund may not withhold its approval of an alteration beyond the initial 10 per cent if it is satisfied that the requested change is necessary to correct a "fundamental disequilibrium;" in particular, if it is so satisfied, it may not refuse a requested alteration because of the domestic social or political policies of the applying member.

There are complicated mechanical provisions designed to enable the Fund regularly to replenish its stock of currencies most in demand; e.g., once a year (with certain exceptions) each member must use part or all of any increase in its monetary reserves (gold and convertible currencies) for the purpose of buying back from the Fund a part of any increase in the Fund's holdings of its currency. In order to discourage unduly prolonged or heavy borrowing from the Fund, there is provision for modest interest charges, on a scale rising with the duration and extent of the borrowing. The Bretton Woods monetary agreement carries over from the Joint Statement the provision for automatic authorization of limitations on the use of a currency of which the Fund runs short, and stipulates that the provisions of previous agreements (such, for instance, as the Hull trade agreements) are not to be invoked for the purpose of preventing such limitations.

The International Bank for Reconstruction and Development, as planned in Bretton Woods, is to have an authorized capital of 10 billion dollars, of which 9.1 billion dollars would be subscribed by the United and Associated Nations. The United States would subscribe 3,175 million dollars, the United Kingdom 1,300 million dollars, the U. S. S. R. 1,200 million dollars, China 600 million dollars, and France 450 million dollars. Only 10 per cent of the capital has to be paid up during the first year (2 per cent in gold or dollars, the rest in local currencies), another 10 per cent is subject to early call, and the remaining 80 per cent is reserved for use in meeting the Bank's obligations in connection with its market borrowings or loan guarantees. The Bank is to have authority to make, participate in, or guarantee loans to central and local governments and to private enterprises in member countries, provided such loans are guaranteed by the respective member government or its central bank, provided the borrower cannot otherwise obtain the loan on reasonable terms, and subject to certain safeguards, such as a careful study of the merits of each proposed loan by a competent committee, which must first submit a written report. It is also provided that, "except in special circumstances", loans made or guaranteed by the Bank shall be for the purpose of specific projects of reconstruction and development. The Bank is to charge a guarantee commission of 1 to 1½ per cent per annum, to be paid, together with commissions earned on direct loans, into a special reserve. Any payments which the Bank may have to make on its guarantees are to come, first, out of the special reserve, and secondly, out of other reserves, surplus and capital.

The provisions with respect to organization and management are almost identical in the Fund and Bank plans. In each case there is to be a Board of Governors, consisting of one governor and one alternate from each member country, which is to meet at least once a year. The Board of Governors is to elect a Chairman and twelve Executive Directors (possibly fourteen, in the case of the Fund), five of the Directors to represent the five countries having the largest participations. The Executive Directors, who are to remain in continuous session, will elect the principal executive officer of each institution (called "Managing Director" in the case of the Fund and "President" in the case of the Bank). The head office of both institutions is to be in the country holding the largest participation, i.e., in the United States, but regional offices and agencies may be opened. Both the Fund and the Bank agreements are to enter into force as soon as ratified by countries subscribing 65 per cent of the total of initially contemplated subscriptions, but not before May 1, 1945, nor after December 31, 1945.

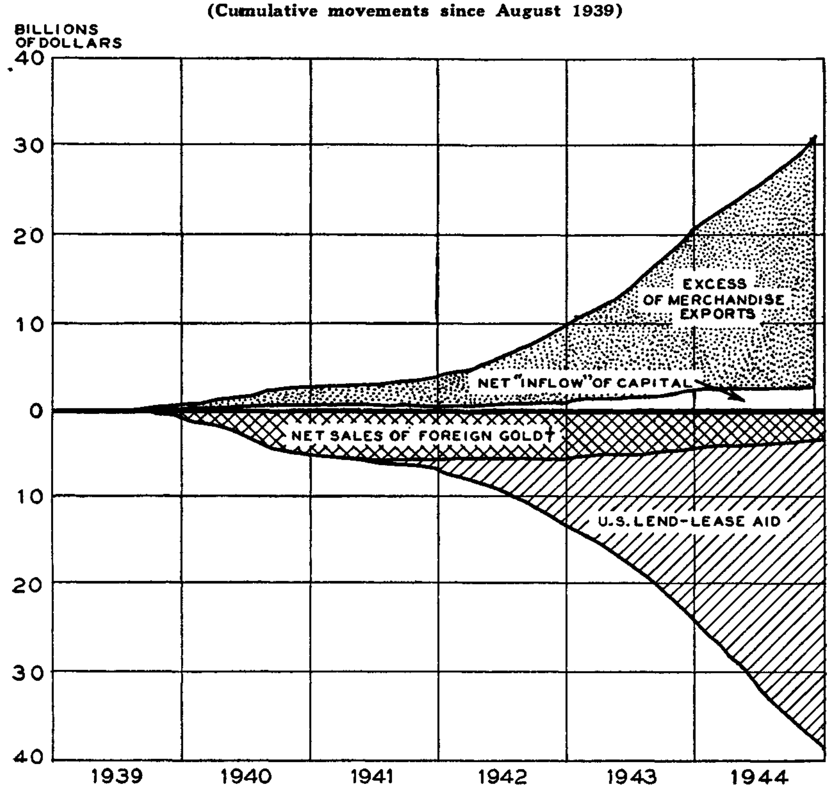
The results of the Bretton Woods conference have had a mixed reception. American opinion, with a few dissenting voices, reacted favorably to the proposal for an International Bank. There was also fairly unanimous agreement in this country on the desirability of the aims to be pursued by the proposed Fund—especially on the desirability of arrangements for international consultation and cooperation to promote greater exchange stability and to reduce barriers to international trade—but there has been much less general agreement on the practical and advantageous working of the Fund, particularly under the abnormal circumstances of the period of transition from war to peace. This has led some of those who recognize the urgent need for the Bank, but who question the urgency of the need for the establishment of the Fund, to suggest that action on the Fund be deferred and that the scope of operations of the Bank be enlarged so as to embrace such currency stabilization functions as they believe can be carried forward successfully in the transition period.

On February 2, 1945, there was introduced in both houses of Congress a bill (the Bretton Woods Agreement Act) to provide for the participation of the United States in both the Monetary Fund and the Reconstruction Bank.

The United States Wartime Balance of International Payments

More than five years of war have brought about far-reaching changes in the United States balance of payments with other countries. The impact of the transition, however, was most pronounced during the period of our neutrality. By the time this country entered the war, the shifts had more or less resolved themselves into a definite wartime pattern. The transition began with the widespread imposition of rigid controls over international finance and trade, which had the effect of directing most international transactions through official channels. Gold transfers between countries were placed largely on a government-to-government

Principal Items in the United States Wartime Balance of Payments with Foreign Countries*
(Cumulative movements since August 1939)



* Areas above the zero line represent two of the principal sources of demand for dollars or their equivalent by foreign countries; areas below the zero line represent the two principal methods by which dollars or their equivalent have been obtained.

† Cumulative gold movements based on changes in U. S. gold stock, exclusive of domestic production.

basis, the movement of capital was determined almost entirely by government policy, and foreign trade began to reflect mainly the flow of war materials rather than an economic exchange of goods.

In the early phase of the transition, this country's balance of payments was dominated by an expansion in merchandise exports, accompanied by a large-scale liquidation, first, of foreign gold reserves, and then of dollar assets, to finance purchases of urgently needed war supplies in the "cash and carry" period of our neutrality. During the first twenty months of the war in Europe this country acquired, on balance, 5.6 billion dollars of foreign gold, or at a monthly average rate of 280 million dollars. Beginning in the early part of 1941 foreign-held dollar assets, particularly the British holdings, were heavily drawn upon and during the thirteen months ended February 1942, foreign funds in this country were reduced by about 625 million dollars.

The first phase of our wartime balance of payments was brought to an end, and the present phase began, with the passage of the Lend-Lease Act, which introduced a new concept of wartime international finance. Since the passage of the Act, the rapidly expanding export of war supplies has been handled largely as a bookkeeping operation and has ceased to be accompanied by a corresponding movement of gold, capital, or both. Supplementing lend-lease aid in relieving the strain on foreign dollar and gold reserves, our cash purchases of vital raw materials abroad, which were stepped up as a result of our defense program even before we entered the war, began to provide many foreign countries with substantial amounts of dollar exchange, and have run to very large amounts subsequently. Cash outlays were further enhanced with the movement of large numbers of our troops overseas, requiring sizable expenditures for goods and services not being supplied under reverse lend-lease.

Trade and Services

From the chart on page 41, which traces the trends since August 1939 in the more important factors making up this country's balance of international payments, it can be seen that merchandise exports have had a phenomenal growth. Although a merchandise export surplus had been a characteristic of the balance of payments of this country for many years prior to the war, the role of the "arsenal of democracy" demanded the shipment of unprecedented amounts of American military equipment to the war fronts and of food and other civilian goods to those countries whose home fronts had to be maintained for the successful prosecution of the war. As the world's largest exporter, this country is currently exporting goods at the rate of about 14 billion dollars a year, or more than four times the prewar level. Since the war in Europe began, a total of about 45 billion dollars of American products has been transported abroad, around 27 billion, or over one half of this amount, during 1943 and 1944.

Not only has the over-all amount of our exports expanded rapidly during the past five years, but there have also been fundamental shifts in the channels of trade. Nearly two thirds of the exports are now going to the United Kingdom and the Union of Soviet Socialist Republics, and sizable additional amounts, accounting for around 10 per cent of total exports, are being shipped to Africa, the Middle East, and the Mediterranean area. Before the war all these regions combined received less than one third of our exports. Exports to the Allied-controlled Far Eastern and Pacific areas have increased about sixfold. A less spectacular, though significant, expansion has occurred in exports to Canada and the Latin American Republics. On the other hand, our trade with the continental European countries, which had taken sizable amounts of our exports before the war, has all but disappeared in recent years.

On the import side, there has also been an expansion in this country's purchases abroad, although the rise has been small in relation to the increase in exports. During 1944, imports — consisting largely of raw materials needed for war production and of essential foodstuffs—totaled nearly 4 billion dollars. This compared with average prewar imports (1936-38) of about 2.5 billion a year. Here too there have been marked shifts in the channels of trade, as new sources of supply have had to be tapped to make up for the loss of areas, largely in the Far East, that have come under enemy control.

The various services rendered foreign countries (which are not shown in the chart) have also increased greatly since the outbreak of hostilities in Europe. Before the war this country was a net debtor on the various service item accounts in the balance of payments. This arose primarily from payments covering American travel abroad, personal remittances, and the use of foreign freight and shipping facilities. These payments were in excess of receipts, which came largely from interest and dividends on our overseas investments. Since the war began, however, our services rendered, chiefly representing rental and repair of ships and other wartime operations, have exceeded services received from abroad.

Lend-Lease and Reverse Lend-Lease

The change in the character of our international finance and trade brought about by the lend-lease program can be seen in the chart on page 41. Prior to lend-lease, the volume of this country's exports was dependent not only upon the foreign need, but also upon the ability of foreign countries to finance their purchases. Under the lend-lease program, the bulk of the American products going abroad, and of the services rendered, is divorced from financial considerations and the shipment of war supplies to the Allies is dependent only upon their needs and the ability to produce and transport the goods. The chart shows clearly the steady, rapid increase in lend-lease assistance, which has taken the place of the previous heavy inflow of gold, as an offset to our merchandise export surplus in the balance of payments. Through December 1944 this aid to our Allies had reached 35.4 billion dollars. This was in addition to nearly 800 million dollars of goods transferred in the field or consigned to commanding generals for subsequent field transfer. Nearly 90 per cent, or 31.4 billion dollars, of the aid represented goods transferred, including 18.1 billion of munitions (including ships) and 13.3 billion of industrial materials and agricultural products. The remainder of the assistance consisted of services, primarily the rental, servicing, and repair of ships.

Of the 30.2 billion dollars of goods transferred through November 1944 (the latest date for which figures on lend-lease exports are available), 26.2 billion had been exported. The United Kingdom has been by far the largest recipient, acquiring a total of 11.3 billion dollars of goods. The United Kingdom during the first eleven months of 1944 received 45 per cent of lend-lease exports, compared with nearly 80 per cent in 1941. The Soviet Union had acquired 7.4 billion dollars of goods through November 1944, while around 3.5 billion had gone to Africa, the Middle East, and the Mediterranean area, and 2.9 billion to China, India, Australia, and New Zealand.

Concurrently with the extension of lend-lease, we received a total of 3.9 billion dollars of reverse lend-lease aid from the British Commonwealth of Nations through September 1944. Nearly one third of this amount was received in the first six months of 1944, when the demands for supplies in preparation for the invasion of Europe were heaviest. The United Kingdom alone furnished 2.8 billion of the aid through September 1944, while, of the remainder, around 650 million dollars came from Australia, 300 million from India, and 150 million from New Zealand.

As a result of the lend-lease program, although total merchandise exports from this country during 1944 amounted to over 1 billion a month, only about 200 to 300 million dollars a month of these goods required cash payment. With the stepping up of imports, our trade balance, on a cash basis, began to show a deficit in December 1942 for the first time since June 1937. From December 1942 through December 1944, imports exceeded cash exports by 1.8 billion dollars. During 1944, the import surplus on a cash basis provided foreigners with nearly 1 billion dollars; furthermore, this amount is in addition to goods which we have purchased and stockpiled abroad. The principal recipients of our cash payments for goods have been the Latin American countries, which during 1944 probably received, on balance, well over 500 million through the excess of our imports over cash exports.

U. S. Government Spending Abroad

The establishment of bases and the concentration of large numbers of American troops abroad have also resulted in placing large actual or, in some cases, potential sources of dollar exchange in the hands of foreign monetary authorities. Whereas our purchases of foreign goods either for import or stockpiling abroad have benefited the Latin American countries and, to a lesser extent, the European neutrals, our European and Asiatic Allies have received the greater part of our outlays in connection with military and naval expenditures abroad. In some cases, local currency is provided American forces against payment in dollars by the United States Government, thus making dollar funds readily available to the various foreign central banks and governments. In other cases, such as Italy, where Army maintenance costs and pay of troops have been financed by the issuance of allied military currency, our outlays result in no concurrent payment of dollars directly to foreign account. In the case of Italy, however, it has been announced that some dollars eventually will be made available for the purchase of goods here.

Foreign Purchases Of Gold

The greater part of the foreign accumulation of dollar exchange resulting from our military and other expenditures abroad has been converted into gold to be earmarked in this country for foreign account, or, in some cases, to be exported. Foreign buying of gold began around the middle of 1941 and by November of that year the purchases had reached sufficient proportions to cause a downturn in our monetary gold stock. Foreign buying continued at a moderate rate until the end of 1942, when conversions of dollar exchange into gold were stepped up substantially. From the October 1941 peak to the end of 1944, the United States gold stock declined 2.2 billion dollars, or about 10 per cent. When gold acquired through domestic production is taken into account, the indicated loss of gold to foreign countries has amounted to around 2.4 billion dollars, or at an average monthly rate of about 65 million dollars.

From the balance of payments point of view, the significance of foreign conversions of dollar exchange into gold lies not only in the amounts purchased, but also in the fact that it has brought about a sustained "outflow" of gold for the first time since 1933. It will be recalled that an unprecedented inflow of gold occurred in the years before and immediately following the outbreak of the war. From the summer of 1938 through the early part of 1941, 9 billion dollars (net) of foreign gold was acquired by the United States. As a result, total foreign gold holdings (excluding those of the U. S. S. R.) by mid-1941 had declined to about 8.2 billion dollars, compared with 22.6 billion dollars held by the United States on the same date. As a result of the gold purchases by foreign monetary authorities since mid-1941, plus new production and other factors, gold reserves of all foreign countries except the U. S. S. R. had been restored to an estimated total of about 13 billion dollars by the end of 1944. This not only has brought about the wiping out of the 1938-1941 decline, but, in the case of many countries, has restored gold reserves to predepression levels in physical amount and to considerably higher levels in dollar value.

It is significant that the individual countries that have recently acquired gold are, for the most part, the same ones which had experienced serious drains on their gold reserves in previous years. This is particularly true of the Latin American Republics, many of which had been obliged to draw heavily on their gold holdings throughout the late 1920's and the

1930's, as well as in the immediate prewar years. The extent of the recovery can be seen from the fact that gold holdings of all the Latin American Republics at the end of 1944 amounted to an estimated 2.3 billion dollars, or more than triple the amount held in August 1939 and nearly 50 per cent above the 1929 level, even after adjustment for the 1934 change in the dollar value of gold.

Published figures indicate large increases in the gold holdings of many of the European neutrals during the last few years. Swiss gold reserves, at 1,052 million dollars in December 1944, and the Swedish gold stock, at 463 million dollars, both stood at record high levels. Compared with the 1940 lows, Swiss reserves have more than doubled, while the Swedish monetary gold stock has increased threefold. On the other hand, gold stocks of our European Allies, some of whom sustained heavy losses in the early war years, are presumably still below prewar levels.

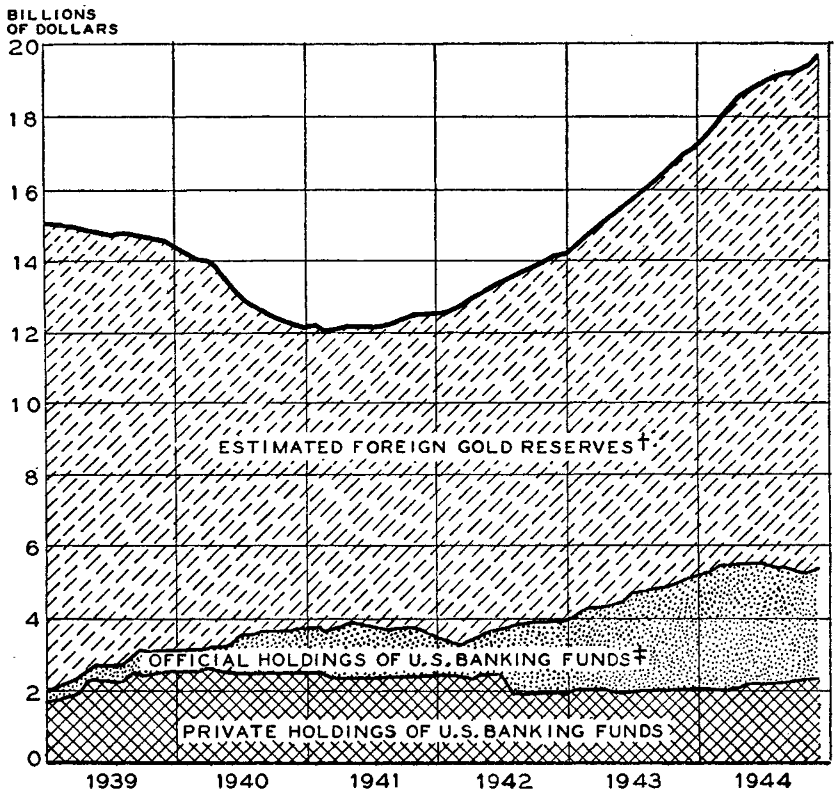
The recent acquisitions of gold seem to reflect principally a desire on the part of many countries to recoup gold reserves lost in the prewar and early war years by using the wartime—and therefore presumably temporary—accumulation of dollar exchange. Legal limitations on the holding of central bank reserves in dollars or in other foreign currencies may have been responsible for gold purchases in some cases. It is also possible that political considerations may have been a factor in a few instances.

In general, the world-wide demand for gold seems to constitute a denial of the expectations expressed only a few years ago that gold would cease to be used for monetary reserves in many countries.

International Capital Movements

Although international capital movements, along with the gold flow, have, in a limited sense, continued to act during wartime as a means of settling differences in the balance of payments, the trend of international capital transfers has been shaped almost entirely by governmental policies, both here and abroad, and by official actions taken to implement the policies. As mentioned earlier, foreign holdings of dollar assets were drawn upon heavily during the pre-lend-lease phase of the war. By February 1942, however, the reduction of foreign funds in this country had halted and dollar exchange again began to accumulate in foreign accounts, as our spending abroad increased and lend-lease aid obviated the need for foreigners to pay cash for the greater part of American exports. Despite the conversion of dollars into gold, foreign holdings of dollars increased with little interruption through March 1944, although the rate of net accumulation diminished as foreign purchases of gold were increased. Between February 1942 and March 1944 the recorded data indicate an "inflow" of capital amounting to 2.4 billion dollars. Of this amount, nearly 2.0 billion represented a building up of short term dollar assets by foreign central banks and governments. As a result, foreign deposits and other banking funds, as of March 1944, amounted to 5.5 billion dollars, of which 3.5 billion belonged to foreign monetary authorities—the largest amount ever held in this country for official foreign account.

Foreign Holdings of Gold and of Banking Funds in the United States



† Foreign gold reserves based on estimated world reserves as of December 31. 1938, *plus* approximate world gold production for subsequent months, *less* United States gold reserves.

‡ Since July 1942, includes funds held for account of foreign central banks, governments, and their agencies; prior to that date, included funds held in New York City for account only of central banks and certain governments. Shift in July 1942 as between private and official holdings due to change in classification.

By April 1944 conversions of dollars into gold began to exceed current accumulations of dollars in official accounts, with the result that the volume of foreign deposits and other banking funds held in this country turned downward. In November 1944, such funds in the United States totaled 5.4 billion, of which 3.2 billion represented official dollar reserves.

Recent years have also witnessed an over-all improvement in foreigners' position with respect to long term dollar assets. From the end of February 1942 through November 1944, foreigners acquired American stocks and bonds in the net amount of 106 million dollars, of which 31 million were purchased during the first eleven months of 1944. In addition, 169 million dollars of foreign securities outstanding in this market were, according to reported data, repurchased prior to maturity or redeemed at maturity. This repatriation, which amounted to 100 million during 1944 alone, was largely for Canadian and Latin American account.

The chart on page 48 shows, by months since the beginning of 1939, private and official foreign holdings of deposits and other banking assets in the United States (excluding stocks, bonds, and other long term investments) and estimated foreign gold reserves. The figures for foreign gold reserves should be considered as only rough estimations, intended to indicate trends rather than to measure accurately the actual amounts.

The two distinct phases in the transition in our international financial operations to a wartime basis are apparent in the movement of these foreign reserves. It can be seen that in the pre-lend-lease period, the combined holdings of deposits and other banking assets and gold dropped about 3 billion dollars to reach a low point in February 1941. From that point, the total rose gradually during the next year and then advanced sharply, as the United States became more actively engaged in the war. From February 1941 through November 1944, the last date for which figures are available, foreign-owned gold and dollar deposits and other banking assets were built up by nearly 8 billion dollars. Nearly 6 billion of this increase was in gold holdings. The remainder represented current acquisitions by foreign monetary authorities of dollars which continued to be held in the form of balances or short term investments.

Privately-held banking assets of foreigners in this country have remained fairly steady at roughly 2 billion dollars in recent years. In large part, this amount represents funds which foreign banks and corporations are permitted, under the exchange regulations in effect abroad, to retain as working balances needed in the conduct of their normal business.

In November 1944 total foreign holdings of gold and dollar deposits and other banking assets were the largest ever held. These reserves should greatly facilitate the establishment of international exchange stability after the war. Whether or not the stability can be maintained, however, will depend upon the ability of foreign nations to bring their international accounts into balance within a reasonable period. It is likely that there will be some absorption of foreign reserves in the transitional period. The belligerents, of course, will have great need for American goods to rebuild devastated areas and to assist in the economic rehabilitation of their countries. Furthermore, they have participated in the wartime accumulation of gold and dollars only to a limited extent, if at all. American products will also be needed by other countries which will have to replace capital equipment and to meet long delayed requirements for consumers' durable goods. Beyond the immediate postwar demands, the economic expansion of undeveloped countries and the exploitation of as yet unused national resources could provide a very large demand for American goods if funds with which to pay for them were available.

The ability of foreign countries to retain even part of their wartime accumulation of dollars and gold, therefore, will depend heavily upon their ability to obtain a large and steady supply of dollars in postwar years, or to control the expenditure of these dollar funds by their nationals for nonproductive imports. The export of American capital through loans and investments abroad may be one important source of supply of dollars, and a necessary one in the immediate postwar period. From the point of view of long term equilibrium in the balance of international payments, however, the real solution lies in the ability of other countries (in the aggregate) to increase their exports of goods and services to us. Only if they are able to reduce, and eventually to eliminate their deficit in trade*, can a continued drain on their monetary reserves be prevented and long-run stability of their exchanges be maintained.

* It is important to note, however, that the term "trade" should be interpreted broadly to include not merely merchandise imports and exports but all international transactions except capital and gold movements.

Foreign Exchanges

Owing to the foreign exchange controls throughout the world, together with the use of various credit arrangements such as lend-lease, foreign exchange trading, on the whole, was uneventful during 1944 and rates in the various exchange markets continued generally to move within narrow limits.

Except for new rates established for the currencies of liberated countries, official rates for the principal foreign exchanges, as maintained by the controls abroad, were unchanged during the year. The pound sterling continued to be quoted officially at \$4.03½ for British purchases of dollars and \$4.02½ for sales of dollars, and no alterations were made in official dollar rates for other sterling area currencies. The Canadian dollar-United States dollar rate was maintained at \$0.9091-\$0.9009 by the Canadian Foreign Exchange Control Board. The rates set for most of the controlled Latin American exchanges likewise continued at previously quoted levels.

Accompanying the Allied liberation of a large portion of Europe and of areas in the Pacific, a number of currency arrangements and rates of exchange to be used by the Allied forces were announced during 1944. In Metropolitan France, the United States Army is using a rate equivalent to \$0.020175 per franc, while in French Africa the rate of \$0.02 continued. The Italian lira has been fixed at \$0.01 for some time. Prior to the suspension of New York trading in these exchanges, the French franc had been quoted at \$0.0218 and the lira at \$0.0526. Although, according to the joint statements of the Treasury and War Departments, no general rate of exchange between the Allied military mark or the reichsmark and the dollar has been established, a provisional rate of 10 marks to the dollar is being used for the purposes of computing troop pay. This rate compares with the pre-freezing rates of about 40 cents for the "free" mark, of about 12 cents for the registered mark, and of about 4 cents to 17 cents for other special types of German exchange.

In the Netherlands and Belgium the liberating forces are being supplied with the local currency of these countries at established rates of exchange. The Netherlands Government selected rates of 2.64957 guilders to the dollar—equivalent to \$0.3774—and of 10.691 to the pound sterling. The Belgian franc-dollar rate was set at 43.773 francs to the dollar, or equivalent to \$0.0228 per Belgian franc. The exchange rates established for the Belgian franc were also made applicable in Luxembourg, at the instance of the Luxembourg Government. The rates for both the guilder and the Belgian franc represent a depreciation of about 30 per cent from the pre-invasion levels.

In August 1944, a monetary agreement was signed between the Belgian and British Governments. In addition to fixing an official rate of exchange of 176⅝ Belgian francs to the pound, the agreement provided that the Belgian Congo would leave the sterling area and be brought into a Belgian monetary area composed of Belgium, Luxembourg, Belgian Congo, and Ruanda Urundi. The accord, which is to remain in force for three years unless terminated earlier by three months' notice given to either party, will be reviewed for possible amendment if the contracting governments adhere to any general international monetary agreement. It was also announced at the time that an agreement had been reached in principle between the British and Royal Netherlands Government for a similar monetary accord.

Following the invasion of the Philippines, it was announced that the United States Army and Navy forces there were using a new "Victory Series" of Philippine currency and a new 1944 series of Philippine coins which had been prepared in anticipation of the liberation. The prewar exchange rate of 2 pesos to the dollar has been resumed by the liberating forces.

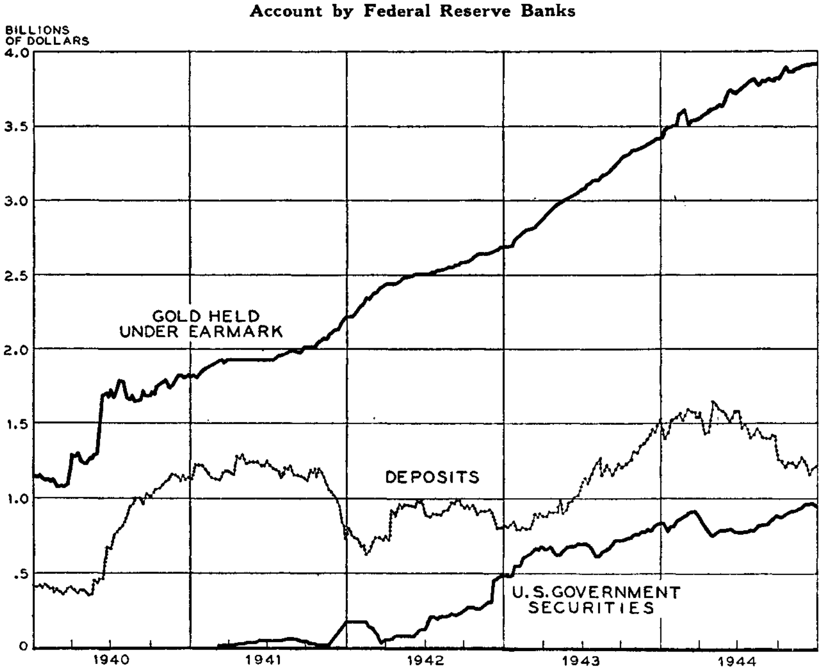
In the New York market, quotations generally reflected closely the official rates established abroad. The unofficial New York quotation for the Canadian dollar rose in the early months of the year, when this exchange was traded at rates as high as $0.9087½; this was only slightly below the rate at which the Canadian control makes Canadian dollars available against United States dollars. Subsequently, however, the unofficial rate declined irregularly, reaching a low of $0.8875 in September and closing the year at $0.8987½, to show only a slight net rise for the year as a whole. New York quotations for most other Western Hemisphere currencies held steady.

The only sizable movement in New York quotations occurred in the so-called free rate for the Swiss franc. It will be recalled that this rate, as distinguished from the so-called official rate of $0.2331 at which Swiss banks supply Swiss exchange against dollars for certain transactions, rose abruptly in the latter part of 1943. By February 1944, this rate had reached a high of slightly over $0.4400. Largely as a result of official sales in this market, the "free" rate subsequently declined sharply and by May had receded to about $0.2350. Except for some temporary appreciation in the latter part of May and in June, the "free" rate held at about this level during the remainder of the year. At the end of December, the rate was quoted at $0.2340, or only slightly above the "official" rate.

Foreign Relations

Continuing the steady, rapid rise of previous years, the total volume of funds (dollar balances, earmarked gold, and United States Government securities and other investments) held by the Federal Reserve Banks for account of foreign central banks and governments rose above 6 billion dollars in February 1944. During the remainder of the year, however, there was little further increase and at the end of December 1944 the total was 6,122 million dollars. This compared with 5,693 million dollars a year earlier, and with only 1,515 million immediately prior to the outbreak of the war. The cessation of the previous rapid rise in

Earmarked Gold, Deposits, and United States Government Securities Held for Foreign Account by Federal Reserve Banks



foreign funds held by the Federal Reserve Banks has been due to a number of developments, including unusually heavy dollar payments by official foreign accounts during the year and a stepping up in the shipment of gold abroad. As a result of the export of gold, although foreign central banks and governments continued to purchase gold to be earmarked here, the total amount of gold held under earmark at the end of 1944, amounting to 3,937 million dollars, showed a net increase for the year of only 460 million dollars. During 1943 earmarked gold rose by 804 million dollars.

Foreign monetary authorities continued during 1944 to keep part of their holdings of dollars in United States Government securities, although the net rise for the year was considerably below the 352 million increase shown in 1943. At the end of the year under review, seven foreign accounts had a total of 960 million dollars invested in United States Government issues, as against 833 million dollars in ten accounts a year earlier. Foreign deposits held by the Federal Reserve Banks reached a high of 1,650 million dollars in May 1944, but by the end of the year had declined to 1,201 million, to show a net reduction of 159 million dollars for the year as a whole.

During 1944 two new foreign accounts were opened on the books of the Federal Reserve Bank of New York, in its capacity as fiscal agent of the United States. In addition, two old accounts held by this bank on its own behalf and that of other Reserve Banks, which had been dormant for some time, became active following the liberation of the countries involved.

This bank, acting as fiscal agent of the United States, established one new foreign currency account with a central bank abroad. No new accounts were opened abroad on behalf of this bank and the other Reserve Banks, and balances in existing accounts remained virtually unchanged during the year.

Operations of the Bank in 1944

Despite further growth in the volume of work handled by the bank during the past year, especially in fiscal agency work related to war expenditures and war financing, the size of the staff appeared to have reached its wartime peak. The total number of employees at the end of 1944 was 4,572, or slightly less than at the close of 1943. The greatest number of employees was reached in July, when the total was close to 4,900. Several factors made it possible to handle an increased volume of work without a net increase in the staff. Among these factors were a reduction of about one third in the rate of turnover in the staff and a consequent gain in experience and efficiency, reduced absenteeism, and finally a change in procedure in the redemption of United States Savings bonds, which had the effect of checking the expansion in the work of the Savings Bond Redemption Department.

Effective October 2, 1944, the Treasury Department authorized incorporated banks and trust companies to qualify to redeem United States Savings bonds of all Series from A through E held by individuals. Over 98 per cent of the banks in this District qualified, and during the last three months of the year by far the greater number of Savings bonds were redeemed by qualified banks. The bonds redeemed in this District continued to be "processed" by this bank for the Treasury, but the bonds were handled more largely in bulk, and transactions with the individual owners were largely shifted to banks throughout the District.

The total number of Government securities issued, redeemed, and exchanged by this bank increased further to more than 53 million pieces representing a total value of nearly 141 billion dollars, compared with 42 million pieces valued at 112 billion dollars in 1943. Included in the securities handled were nearly 38 million Savings bonds with a face value of 2.2 billion dollars issued to issuing agents in the District, compared with 32 million bonds with a face value of 2.0 billion in 1943. Other securities issued during the year totaled 1,200 thousand pieces with a face value of 75 billion dollars, compared with 900 thousand pieces with a face value of 58 billion dollars in 1943.

The securities safekeeping function of the bank had a corresponding expansion in its operations during the past year. Receipts and deliveries of securities for the Treasury, for member banks, and for others totaled more than 86 million pieces with a par value of 488 billion dollars in

1944, compared with about 75 million pieces with a par value of 435 billion in 1943.

Among other fiscal agency operations handled by this bank, the greatest increase during the past year was in the handling of United States Government checks. The total number of such checks handled in 1944 was close to 94 million compared with 61½ million in the previous year. The number of United States Government coupons paid also showed a further increase, though of much smaller proportions than the increase in Government checks.

A large volume of operations was also performed by this bank as fiscal agent of the Reconstruction Finance Corporation and its subsidiaries and the Commodity Credit Corporation, although there was a moderate reduction from 1943 which is best measured by the dollar volume of transactions shown in the lower part of the table. (The reduction in the number of disbursements shown in the upper part of the table—178,000 in 1944 compared with 455,000 in 1943—is misleading, as the figure for 1943 included a large number of checks issued in payment for spare automobile tires which the owners were required to turn in during the latter part of 1942, payments for which extended well into 1943).

The number of applications for Regulation V loans (War Production Loans) received during 1944 was substantially less than in 1943. Furthermore, relatively few concerns have availed themselves, thus far, of the facilities afforded under the Contract Settlement Act of 1944 for adequate interim financing (through "T" loans) of war contractors who may have termination claims. While the partial payment plan may serve fairly well the needs of prime contractors and first-tier subcontractors, it is doubtful whether it will meet the needs of subcontractors in the lower tiers. It would be unfortunate, after the lending machinery has been provided, if, because of inadequate information or lack of foresight, such war contractors failed to avail themselves of the opportunity to obtain commitments for "T" loans.

The work of the Foreign Funds Control Department diminished further in the early part of the year, but the decline in applications for licenses was checked after the resumption of communications with liberated areas was permitted, resulting in an increase of the number of applications for transactions involving the nationals of those areas.

Some Measures of the Volume of Operations of the Federal Reserve Bank of New York

	1944	1943
Number of pieces handled*		
Discounts and advances	2,000	940
Currency received and counted	803,124,000	759,332,000
Coin received and counted	1,474,796,000	1,441,589,000
Checks handled:		
United States Government checks	93,956,000	61,568,000
All other	231,733,000	224,249,000
Collection items handled:		
United States Government coupons paid**	5,716,000	5,466,000
All other	1,111,000	1,310,000
Disbursements as fiscal agent for Reconstruction Finance Corporation, its subsidiaries, and Commodity Credit Corporation	178,000	455,000
Issues, redemptions, and exchanges by fiscal agency departments:		
United States Government direct obligations	53,343,000	42,090,000
All other	330,000	182,000
Safekeeping of securities:		
Pieces received and delivered	86,438,000	74,906,000
Coupons detached	1,069,000	2,255,000
Wire transfers of funds	167,000	158,000
Incoming and outgoing mail:		
Registered	2,194,000	2,391,000
Ordinary	15,767,000	17,187,000
Amounts handled		
Discounts and advances	$11,036,595,000	$642,816,000
Currency received and counted	5,012,560,000	4,439,525,000
Coin received and counted	144,082,000	138,784,000
Checks handled:		
United States Government checks	34,534,949,000	32,483,158,000
All other	144,130,545,000	139,355,654,000
Collection items handled:		
United States Government coupons paid**	1,162,032,000	932,461,000
All other	2,476,282,000	2,407,785,000
Disbursements as fiscal agent for Reconstruction Finance Corporation, its subsidiaries, and Commodity Credit Corporation	1,797,796,000	1,953,292,000
Issues, redemptions, and exchanges by fiscal agency departments:		
United States Government direct obligations	140,914,520,000	112,431,087,000
All other	2,099,760,000	1,753,839,000
Safekeeping of securities:		
Pieces received and delivered (par value)	488,272,594,000	434,560,313,000
Wire transfers of funds	62,873,298,000	62,527,138,000

* Two or more checks, coupons, etc., handled as a single item are counted as one "piece."

** Includes coupons from obligations guaranteed by the United States.

The ordinary operations of the bank, such as supplying currency to meet public demands in the District, the handling of non-Government checks, etc., also showed further expansion during 1944. The number of pieces of paper currency issued, for example, was 8 per cent greater than in 1943, and the number of pieces received was 10 per cent greater. The greater increase in receipts than in payments apparently reflected a tendency to use bills of larger denominations; the number of bills of $50 and greater denomination issued was 23 per cent greater than in 1943, the largest increase being in the $100 denomination. The general increase in volume of currency in use was also reflected in an increase in the number and amount of coins issued and received.

Financial Statements

Statement Of Condition

War financing and money market events during 1944 are reflected in the changes shown in the items of the statement of condition of the Federal Reserve Bank of New York. Continuing the trend of the past

(In thousands of dollars)

Assets	Dec. 31, 1944	Dec. 31, 1943
Gold certificates on hand and due from U. S. Treasury	$ 5,149,403	$ 5,904,288
Redemption Fund—Federal Reserve notes	106,731	22,844
Other cash	57,125	74,244
Total reserves	$ 5,313,259	$ 6,001,376
Discounts and advances	$ 77,775	$ 2,185
Industrial loans	$ 12	$ 126
U. S. Government securities:		
Bills	$ 2,259,370	$ 2,474,891
Certificates	1,622,723	271,407
Notes	520,764	74,569
Bonds	412,908	179,243
Total U. S. Government securities, (including guaranteed securities)	$ 4,815,765	$ 3,000,110
Total loans and securities	$ 4,893,552	$ 3,002,421
Due from foreign banks	$ 49*	$ 56*
Federal Reserve notes of other banks	17,759	12,394
Uncollected items	569,682	502,634
Bank premises	8,894	9,121
Other assets	16,460	9,936
Total assets	$10,819,655	$ 9,537,938
* After deducting participation of other Federal Reserve Banks	$ 86	$ 80

few years, the reserves of this bank declined nearly 700 million dollars during 1944, making a total reduction of about 4.5 billion dollars since the end of 1940. The loss of reserves was occasioned by sales of gold to foreign countries, and large outward transfers of funds for the Treasury and for commercial and financial purposes, which were only partly offset by payments from the other Federal Reserve Banks for their participation in the System Open Market Account purchases of United States Government securities in the New York market.

The sizable increase during 1944 in discounts and advances, representing member bank borrowings, was only partly reflected in the year-end figure of $77,775,000. During the last three months of the year demands for currency, together with a shift of deposits from reserve-exempt War Loan accounts to private accounts, and transfers of funds to other districts, caused member banks to borrow substantial amounts, particularly in New York City, in order to meet their reserve require-

(In thousands of dollars)

Liabilities	Dec. 31, 1944	Dec. 31, 1943
Federal Reserve notes	$ 4,851,017	$ 3,766,861
Deposits:		
Member bank—reserve account	$ 4,554,844	$ 4,263,922
U. S. Treasurer—General Account	175,050	210,279
Foreign	466,212*	600,236*
Other	287,547	246,308
Total deposits	$ 5,483,653	$ 5,320,745
Deferred availability items	$ 319,639	$ 301,754
Other liabilities including accrued dividends	1,139	1,154
Total liabilities	$10,655,448	$ 9,390,514
Capital accounts:		
Capital paid in	$ 59,282	$ 57,440
Surplus (Section 7)	84,903	70,012
Surplus (Section 13b)	7,142	7,092
Other capital accounts	12,880	12,880
Total capital accounts	$ 164,207	$ 147,424
Total liabilities and capital accounts	$10,819,655	$ 9,537,938
Ratio of total reserves to deposit and Federal Reserve note liabilities combined	51.4%	66.0%
Commitments to make industrial loans	$ —	$ 9
* After deducting participation of other Federal Reserve Banks	$ 735,225	$ 759,843

ments; on one occasion, November 29, just prior to the issue date for the Government securities offered in the Sixth War Loan, borrowings for all member banks in this District reached $464,000,000, the largest amount since March 1933.

Holdings of United States Government securities increased by 1.8 billion dollars, compared with 1.3 billion during 1943, reflecting this bank's participation in the large volume of securities purchased for System Open Market Account during the year. These purchases by the Federal Reserve Bank of New York were made to supply member banks with reserves needed to meet the continued demand for currency, increased reserve requirements, and losses of funds through foreign transactions and transfers to other districts.

The persistent, heavy demand for currency is reflected in the further increase of more than 1 billion dollars in the Federal Reserve notes of this bank in circulation. The deposit liabilities of the Federal Reserve Bank of New York did not change materially between December 31, 1943 and December 31, 1944, although the member bank reserve account increased moderately, reflecting higher reserve requirements caused by the continued growth in member bank deposits.

The drop in the reserve ratio of this bank to 51.4 per cent on December 31, 1944, from 66.0 per cent on December 31, 1943, 80.2 per cent at the end of 1942, and 93.8 per cent at the end of 1941, reflects mainly the shrinkage in the bank's reserves and the large increase in notes in circulation, although growth in deposit liabilities has also been a factor.

Income And Disbursements

The continued expansion of the portfolio of Government securities held by this bank (as well as other Federal Reserve Banks) brought about a substantial increase in gross earnings of the bank—from $17,998,000 in 1943 to $28,993,000 in 1944. While earnings on loans increased considerably, they made up only a small part of gross earnings.

Net expenses increased $1,411,000 to a total of $11,445,000, leaving current net earnings of $17,548,000, an amount $9,584,000 greater than in 1943. The rise in net expenses mainly reflected increases in aggregate compensation of employees and in the cost of supplying Federal Reserve notes, coincident with the heavy demands for currency.

Since this bank's open market operations during 1944 were centered chiefly in short term Government obligations, and involved more purchases than sales, gross profits on securities sold were only $829,000, compared with $10,217,000 for 1943 when substantial sales of longer term securities were made for market stabilization purposes. Other additions of $133,000 to earnings represented recoveries on industrial advances previously charged off and reductions in reserves which had been set up against such items. There were no sizable deductions from current net earnings, such as were made in 1943.

Net earnings amounted to $18,505,000, or $3,174,000 more than in 1943. The usual 6 per cent dividend to stockholders, amounting to $3,483,000, was paid to member banks, and the greater part of the remaining net earnings was transferred to the bank's surplus.

Profit and Loss Account

For the Calendar Years 1944 and 1943

(In thousands of dollars)

	1944	1943
Earnings	$ 28,993	$ 17,998
Net expenses	11,445	10,034
Current net earnings	$ 17,548	$ 7,964
Additions to current net earnings:		
Profits on sales of U.S. Government securities	$ 829	$ 10,217
All other	133	28
Total additions	$ 962	$ 10,245
Deductions from current net earnings:		
Retirement system	$ —	$ 2,389
Special reserve on bank premises	—	482
All other	5	7
Total deductions	$ 5	$ 2,878
Net earnings	$ 18,505	$ 15,331
Paid United States Treasury (Section 13b)	$ 80	$ 18
Dividends paid	3,483	3,280
Transferred to surplus (Section 13b)	51	22
Transferred to surplus (Section 7)	14,891	12,011
Surplus (Section 7) beginning of year	$ 70,012	$ 58,001
Addition as above	14,891	12,011
Surplus (Section 7) end of year	$ 84,903	$ 70,012

Membership Changes in 1944

As in 1943, wartime developments during the past year continued to bring nonmember banks into closer contact with this bank and strengthened a desire on the part of a number of them to obtain the advantages of membership in the Federal Reserve System. The continued growth in membership is reflected in the accompanying table, which shows that 21 State banks and trust companies in the Second Federal Reserve District were admitted to membership during 1944. This was the largest number admitted since 1941, and at the year end total membership of these banks represented 65 per cent of all State banks and trust companies in the District. Including national banks, 85 per cent of commercial banks in this District are members and, measured by total assets, member banks represent about 95 per cent of the assets of all commercial banks in the District. Mergers of 10 member banks with other member or nonmember banks occurred during the year, so that the total membership at the end of the year was 817 out of a total of 956 commercial banks and trust companies in the District.

Number of Member and Nonmember Banks in Second Federal Reserve District at End of Year*
(Exclusive of Savings banks and Industrial banks)

Type of bank	December 31, 1944			December 31, 1943		
	Members	Non-members	Per cent members	Members	Non-members	Per cent members
National banks	558	0	100	565	0	100
State banks and trust companies	259	139	65	241	161	60
Total	817	139	85	806	161	83

Changes in Federal Reserve Membership in Second District During 1944

Total membership beginning of year	806
Increases:†	
State banks and trust companies admitted	21
Decreases:	
Member banks combined with other members	7
Member banks combined with nonmembers	3
Total decreases	10
Total membership end of year	817

* This represents only banks in actual operation.

† In addition to figures shown in this table, one nonmember was absorbed by member during the year.

Geographically, 16 of the new members are located in New York State, 3 in New Jersey, and 2 in Connecticut. A list of State banks and trust companies admitted to membership during 1944 follows.

State Banks and Trust Companies in the Second Federal Reserve District Admitted to Membership in the Federal Reserve System during 1944

		Effective Date
State banks		
Asbury Park, N. J.	Asbury Park and Ocean Grove Bank	October 2
Ebenezer, N. Y.	The Ebenezer State Bank	December 29
Freeport, N. Y.	The Freeport Bank, of Freeport, New York	March 8
Great Kills, N. Y.	The South Shore Bank of Staten Island	September 14
Lake Luzerne, N. Y.	The Luzerne-Hadley Bank	August 14
Lyndonville, N. Y.	Citizens State Bank	January 15
Madrid, N. Y.	Madrid Bank	August 26
Malverne, N. Y.	The Bank of Malverne	February 15
Manlius, N. Y.	Bank of Manlius	May 5
Monroe, N. Y.	Citizens Bank of Monroe	April 25
Newfane, N. Y.	State Bank of Newfane	January 15
Phoenix, N. Y.	The Phoenix Bank	March 15
Trust companies		
Bridgeport, Conn.	The Black Rock Bank and Trust Company	March 16
Bridgeport, Conn.	The Bridgeport-City Trust Company	September 14
Clifton, N. J.	Clifton Trust Company	February 18
Elizabeth, N. J.	Union County Trust Company	September 13
Great Neck Plaza, N. Y. (P.O. Great Neck, N. Y.)	Great Neck Trust Company	March 6
Jamestown, N. Y.	Union Trust Company of Jamestown, N. Y.	November 2
Johnstown, N. Y.	The Johnstown Bank	February 25
Johnstown, N. Y.	The Peoples Bank of Johnstown, N. Y.	May 10
Oyster Bay, N. Y.	North Shore Bank Trust Company	April 26

Changes in Directors and Officers

In August 1944, Frederick E. Williamson, President, The New York Central Railroad Company, New York, N. Y., resigned as a director of this bank because of ill health. Mr. Williamson's subsequent death was a real loss to the bank and to the community.

In the autumn of 1944, at a regular election held by the member banks in Group 2, Harry H. Pond, President, The Plainfield Trust Company, Plainfield, N. J., was elected a Class A director for a term of three years, beginning January 1, 1945, to succeed William J. Field, President, Commercial Trust Company of New Jersey, Jersey City, N. J., whose term expired December 31, 1944. At the same time, Charles E. Adams, Chairman, Air Reduction Company, Inc., New York, N. Y., was elected a Class B director of this bank, for a term of three years, beginning January 1, 1945, to succeed Mr. Williamson.

In December 1944, the Board of Governors of the Federal Reserve System reappointed Beardsley Ruml, Treasurer, R. H. Macy & Co., Inc., New York, N. Y., a Class C director of this bank for a term of three years, beginning January 1, 1945, and redesignated him Chairman and Federal Reserve Agent for the year 1945; the Board of Governors also redesignated William I. Myers as Deputy Chairman of this bank for the year 1945.

In December 1944, the Board of Governors of the Federal Reserve System reappointed Marion B. Folsom, Treasurer, Eastman Kodak Company, Rochester, N. Y., a director of the Buffalo Branch for a term of three years, beginning January 1, 1945.

The directors of this bank appointed George H. Bangert, President, The First National Bank of Kenmore, Kenmore, N. Y., a director of the Buffalo Branch for a term of three years, beginning January 1, 1945, to succeed Robert R. Dew, whose term expired December 31, 1944. The directors of this bank also appointed Gilbert A. Prole as Chairman of the Buffalo Branch for the year 1945, to succeed Marion B. Folsom, and appointed Insley B. Smith, formerly Manager of the Government Check Department at the head office, as Managing Director of the Buffalo Branch for the year 1945, to succeed Reginald B. Wiltse, who was appointed a Vice President at the New York office.

Changes In Officers

Edwin C. French, Manager of the Collection Department, and William M. Kettner, Manager of the Security Custody Department, each of whom had been with the bank for more than 25 years, retired from active service with this bank on March 31, 1944. Effective April 1, 1944, the Board of Directors appointed William F. Abrahams, formerly Chief of the Security Custody Division, Security Custody Department, and Roy E. Wendell, formerly Chief of the Transit Division, Check Department, as Managers, and they were assigned to the Security Custody Department and the Collection Department, respectively.

George W. Ferguson, Assistant Vice President, and a member of the staff since 1917, died on October 14, 1944.

On October 31, 1944, Ray M. Gidney, an officer of this bank since 1917, resigned as Vice President to assume his duties as President of the Federal Reserve Bank of Cleveland, Cleveland, Ohio.

In December 1944, it was announced that effective January 1, 1945, Reginald B. Wiltse, formerly Managing Director of the Buffalo Branch, had been appointed a Vice President of this bank at the head office, and assigned to direct member bank supervision and member bank relations. Insley B. Smith, formerly Manager of the Government Check Department, was appointed Managing Director of the Buffalo Branch to succeed Mr. Wiltse.

In December 1944, Norris O. Johnson, Manager, Research Department, was granted a leave of absence from the bank to join the American Financial Mission in Iran.

Effective January 5, 1945, Harold V. Roelse, formerly Assistant Vice President, was appointed a Vice President of this bank; Harold A. Bilby, formerly Manager, Check Department, Felix T. Davis, formerly Manager, R. F. C. Custody Department, and John H. Wurts, formerly Manager, Government Bond Department, were appointed Assistant Vice Presidents.

Effective at the same time, Curtis R. Bowman, formerly Chief, Credit Division, Credit Department, was appointed Manager of the Credit Department; James J. Carroll, formerly Chief, Planning Division, Accounting Department, was appointed Manager of the newly created Planning Department; and Ralph W. Scheffer, formerly in the Research Department, was appointed Manager of the Check Department.

Member Of Federal Advisory Council

In January 1945, the Board of Directors of this bank reappointed John C. Traphagen, President of the Bank of New York, New York, N. Y., to serve during the year 1945 as the member of the Federal Advisory Council for the Second Federal Reserve District.

Directors and Officers

DIRECTORS

Class	Group		Term Expires Dec. 31
A	1	S. Sloan Colt President, Bankers Trust Company, New York, N. Y.	1946
A	2	Harry H. Pond President, The Plainfield Trust Company, Plainfield, N. J.	1947
A	3	Warren W. Clute, Jr. President, Glen National Bank of Watkins Glen, Watkins Glen, N. Y.	1945
B	1	Donaldson Brown Vice Chairman of the Board, General Motors Corporation, New York, N. Y.	1946
B	2	Charles E. Adams Chairman, Air Reduction Company, Inc., New York, N. Y.	1947
B	3	Carle C. Conway Chairman of the Board and President, Continental Can Company, Inc., New York, N. Y.	1945
C		Beardsley Ruml, *Chairman* Treasurer, R. H. Macy & Co., Inc., New York, N. Y.	1947
C		William I. Myers, *Deputy Chairman* Dean, New York State College of Agriculture, Cornell University, Ithaca, N. Y.	1945
C		Robert D. Calkins Dean, School of Business, Columbia University, New York, N. Y.	1946

DIRECTORS—BUFFALO BRANCH

	Term Expires Dec. 31
Gilbert A. Prole, *Chairman* Farmer, Batavia, N. Y.	1945
Thomas Robins, Jr. President, Hewitt Rubber Corporation, Buffalo, N. Y.	1946
Marion B. Folsom Treasurer, Eastman Kodak Company, Rochester, N. Y.	1947
Lewis G. Harriman President, Manufacturers and Traders Trust Company, Buffalo, N. Y.	1945
Elmer B. Milliman President, Central Trust Company Rochester, N. Y., Rochester, N. Y.	1946
George H. Bangert President, The First National Bank of Kenmore, Kenmore, N. Y.	1947
Insley B. Smith, *Managing Director*	1945

MEMBER OF FEDERAL ADVISORY COUNCIL

John C. Traphagen,
President, Bank of New York,
New York, N. Y.

OFFICERS

ALLAN SPROUL, *President*

LESLIE R. ROUNDS, *First Vice President*
J. WILSON JONES, *Vice President*
L. WERNER KNOKE, *Vice President*
WALTER S. LOGAN, *Vice President, and General Counsel*
ARTHUR PHELAN, *Vice President*
JAMES M. RICE, *Vice President*
HAROLD V. ROELSE, *Vice President*
ROBERT G. ROUSE, *Vice President*
JOHN H. WILLIAMS, *Vice President*
VALENTINE WILLIS, *Vice President*
REGINALD B. WILTSE, *Vice President*

HAROLD A. BILBY, *Assistant Vice President*
FELIX T. DAVIS, *Assistant Vice President*
EDWARD O. DOUGLAS, *Assistant Vice President*
HERBERT H. KIMBALL, *Assistant Vice President*
SILAS A. MILLER, *Assistant Vice President*
HORACE L. SANFORD, *Assistant Vice President*
WILLIAM F. SHEEHAN, *Chief Examiner*
TODD G. TIEBOUT, *Assistant General Counsel*
RUFUS J. TRIMBLE, *Assistant General Counsel*
JOHN H. WURTS, *Assistant Vice President*

WILLIAM F. ABRAHAMS, *Manager, Security Custody Department*
LOREN B. ALLEN, *Manager, Accounting Department*
DUDLEY H. BARROWS, *Manager, Cash Department*
CURTIS R. BOWMAN, *Manager, Credit Department*
HARRY M. BOYD, *Manager, Savings Bond Redemption Department*
ROBERT H. BROME, *Assistant Counsel, and Assistant Secretary*
WESLEY W. BURT, *Manager, Government Bond Department*
JAMES J. CARROLL, *Manager, Planning Department*
NORMAN P. DAVIS, *Manager, Foreign Funds Control Department, and Manager, Security Loans Department*
MARCUS A. HARRIS, *Manager, Securities Department*
WILLIAM A. HEINL, *Manager, Personnel Department*
DANIEL J. LIDDY, *Manager, Foreign Department*
MICHAEL J. MCLAUGHLIN, *Manager, Service Department*
FRANKLIN E. PETERSON, *Manager, Bank Relations Department*
RALPH W. SCHEFFER, *Manager, Check Department*
FREDERICK STOCKER, *Manager, Cash Custody Department*
WILLIAM F. TREIBER, *Assistant Counsel, and Secretary*
CHARLES N. VAN HOUTEN, *Manager, Safekeeping Department*
ROY E. WENDELL, *Manager, Government Check Department*

WILLIAM H. DILLISTIN, *General Auditor*
DONALD J. CAMERON, *Assistant General Auditor*

OFFICERS—BUFFALO BRANCH

INSLEY B. SMITH, *Managing Director*
HALSEY W. SNOW, *Cashier*
GEORGE J. DOLL, *Assistant Cashier*